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No. 20526 ✓

United States
COURT OF APPEALS
for the Ninth Circuit

SCHNITZER STEEL PRODUCTS CO.,
a corporation,

Appellant,

v.

AMTRO CORPORATION, S.A., a Panamanian
corporation, and CIA. ESTRELLA BLANCA, LTDA.,
as Owner of the SS NICTRIC,

Appellees.

AMTRO CORPORATION, S.A.,
a Panamanian corporation,

Cross-Appellant,

v.

SCHNITZER STEEL PRODUCTS CO.,
a corporation, and
CIA. ESTRELLA BLANCA, LTDA.,
as Owner of the SS NICTRIC,

Cross-Appellees.

OPENING BRIEF OF APPELLANT,
SCHNITZER STEEL PRODUCTS CO.

*Upon Appeal from the United States District Court
for the District of Oregon*

HONORABLE JOHN F. KILKENNY, Judge

GUNTHER F. KRAUSE,
CARL R. NEIL,
KRAUSE, LINDSAY & NAHSTOLL,

Ninth Floor, Loyalty Building,
Portland, Oregon 97204,

*Proctors for Appellant,
Schnitzer Steel Products Co.*

STEVENS-NESS LAW PUB. CO., PORTLAND, ORE.

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**OPENING BRIEF OF APPELLANT,
SCHNITZER STEEL PRODUCTS CO.**

*Upon Appeal from the United States District Court
for the District of Oregon*

HONORABLE JOHN F. KILKENNY, Judge

JURISDICTION

This is an appeal from a final decree (R. 152, et seq.) entered on June 18, 1965, by the Hon. John F. Kilkenny sitting in admiralty in the District Court for the District of Oregon. The decree awarded libelant, as owner of the SS NICTRIC, a total of \$48,434.57, plus interest and costs, against Amtro Corporation S. A., the time charterer, for unpaid charter hire and other sums found due under the time charter and as damages for breach of it. Libelant's award ran also against Schnitzer Steel Products Co., as voyage charterer and garnishee. The decree awarded Amtro on its cross-libel against Schnitzer a total of \$62,807.10, plus interest and costs, for demurrage, unpaid freight and stevedore damage, all arising out of a shipment of scrap on the NICTRIC from the United States to Japan in 1961. The decree, however, denied Amtro's claim against Schnitzer for consequential damages for alleged breach of the voyage charter party and misrepresentation.

The District Court had jurisdiction of the cause in admiralty under 28 U.S.C.A. Sec. 1333(1), upon the vessel owner's libel in personam against Amtro and in rem against the subfreights and demurrage monies allegedly owed by Schnitzer (R. 1) and under Amtro's cross-libel against Schnitzer for unpaid freight, demurrage and other sums allegedly due (R. 15).

Timely notice of appeal to this Court from the decree of the District Court was filed by Schnitzer Steel Products Co. on July 19, 1965 (R. 187) and by Amtro Corporation S.A. on August 6, 1965 (R. 193). This

Court has jurisdiction of the appeal under 28 U.S.C.A. Sec. 1291.

STATEMENT OF THE CASE

Libelant is owner of the SS NICTRIC, a tramp vessel under Lebanese registration. Libelant entered on July 23, 1961, a time charter (Ex. 1) of the vessel to Amtro Corporation S. A., a Panamanian corporation with offices in Los Angeles. The vessel was delivered to Amtro at San Francisco on August 6, 1961, and charter hire commenced the following day (R. 103).¹

Amtro at this time was a new company hoping to establish a service between the West Coast and the Far East. The charter of the NICTRIC was its first venture (Tr. 31). It retained the services of a San Francisco charter broker, Ray Kimberk, to arrange a cargo for the vessel (Tr. 32). He contacted Seacharter Company, a Portland charter broker, and negotiations were entered for a voyage charter of the vessel to Schnitzer on a cargo of scrap from the West Coast to Japan (Ex. 79, p. 5 et seq.; Tr. 176 et seq.). It is disputed whether Seacharter Company was acting as an agent of Schnitzer in these negotiations, or acting, instead, as an independent charter broker.

In any event, Schnitzer furnished to Seacharter as a sample for discussion a previous charter party entered by Schnitzer for a scrap cargo shipped on the SS

¹ Libelant will be referred to in this brief as "Owners," the time charterer as "Amtro," and the voyage charterer as "Schnitzer." Page references preceded by "R." refer to the trial court file, and those preceded by "Tr." refer to the transcript of the trial proceedings.

KEHREA (Tr. 177). The provisions of this charter party pertaining to demurrage, including modifications and additions to the original printed language in the charter form, were substantially identical to the charter party finally agreed upon for the NICTRIC (see Exs. 76, 2; Tr. 200). Seacharter sent the KEHREA sample to Amtro by letter dated July 14, 1961 (Ex. 76).

The voyage charter party between Amtro and Schnitzer for the NICTRIC (Ex. 2) is dated July 14, 1961, but was actually signed by Schnitzer on July 25, 1961, and by Amtro shortly after that (Tr. 148-149; Ex. 77). The voyage charter was, of course, for the entire capacity of the vessel, carrying a cargo of scrap from Oregon and British Columbia ports to Japan. Ninety per cent of freight was prepaid, the balance payable upon completion of discharge (R. 105).

Loading of the vessel commenced at New Westminster, B. C., on August 10, 1961, and was completed at Portland on August 26, 1961 (R. 105-106). The vessel arrived in Tokyo harbor and gave notice of readiness to discharge on September 18, 1961 (R. 105). Discharge of scrap there is normally from a berth in the harbor into lighters. Due to congested harbor conditions, the vessel did not receive a discharge berth in the harbor until December 3, 1961 (R. 105), some two and one-half months after her arrival in Japan. Discharge commenced on that date and was completed on December 31, 1961 (R. 105).

Under Clause 18 of the voyage charter, cargo was to be loaded, stowed and discharged within a total of 23 weather working days of 24 hours, Sundays and

holidays excepted unless used, in which case actual time used was to count (R. 105). Under Clause 19, time from noon Saturday until 8:00 a.m. Monday was also not to count unless used. If a longer time than the agreed laydays was used, demurrage was to accrue at the rate of \$700 per day (R. 105). No demurrage was incurred in the loading of the vessel, and the demurrage controversy arises entirely out of delay at the discharge port in Japan. It is agreed that the vessel's lay time expired on October 9, 1961, at 1218 hours, and that demurrage began to accrue on that date (R. 105).

The question of Schnitzer's liability for any demurrage at the unloading port involves interpretation of the following clauses of the voyage charter party (Ex. 2) :

"7. Demurrage, if incurred, to be paid by Charterers, at the rate of Seven Hundred Dollars (\$700) per day or pro rata for any part of a day.

8. Owners shall have a lien on the cargo for freight, dead-freight, demurrage. Charterers shall remain responsible for dead-freight and demurrage, incurred at port of loading. Charterers shall also remain responsible for freight, and demurrage incurred at port of discharge, *but only to such extent as the Owners have been unable to obtain payment thereof by exercising the lien on the cargo.* [emphasis supplied]

.

18. Cargo is to be loaded stowed and discharged within a total of twenty-three (23) weather working days of 24 hours. Sundays and holi-

days excepted unless used, in which case actual time used to count. If longer detained, Charterers to pay demurrage at the rate stipulated in Clause 7 and payments to be made in the same currency as freight payment . . .”

Clause 8 is referred in the lower court proceedings and will be discussed here as the “cesser” or “lien” clause.

The question of Schnitzer’s liability for demurrage on weekends and holidays at the unloading port involves interpretation of Clause 19 of the voyage charter party:

“19. Time from noon Saturday until 8:00 A.M. Monday not to count unless used, in which case actual time used to count. Time from midnight preceding holiday until 8:00 A.M. the day after holiday not to count, unless used, in which case actual time used to count.”

The trial court held that this clause applied only during the laydays, and therefore included demurrage for all weekends and holidays in the total demurrage award of \$57,757.10 against Schnitzer (R. 144-145, 153). It is agreed that the demurrage charges attributable to weekends and holidays included in the award were \$12,483.00 (R. 105-106).

The NICTRIC cargo was sold by Schnitzer under eight contracts of sale to Japanese buyers (Exs. 16, 18-20, 109-112). The terms of all contracts provided for buyers or receivers of the cargo being responsible for discharge of the cargo from the vessel, with one possible exception (Ex. 110). The contracts with only two of the buyers expressly mentioned liability for de-

demurrage at the discharge port. The Okaya company in its contract (Ex. 112) expressly assumed liability for such demurrage, while the Mitsui contracts (Exs. 18 and 19) stated that demurrage at the discharge port was for seller's account.

The ten bills of lading (Exs. 4-13) covering the entire cargo, however, expressly incorporated the terms of the voyage charter party, including, of course, the lien or cesser clause above quoted. Four of the sale contracts expressly provided that charter party bills of lading were acceptable, thus contemplating the incorporation (Exs. 16, 109, 111, 112).

It is agreed that there are unpaid freight charges in the amount of \$4,550 (R. 105).

The opinion of the District Court, embodying its findings and conclusions, is reported as *Cia. Estrella Blanca, Ltda v. SS NICTRIC*, 247 F. Supp. 161 (1965). The Court held that Clause 18 of the voyage charter party modified and superseded Clause 8, so that the latter was ineffective and that no lien on the cargo was given for unloading demurrage and unpaid freight. This, of course, led to the Court's conclusion that inability to exercise the lien was not a condition to Schnitzer's liability for unloading demurrage and unpaid freight, as provided in Clause 8 (R. 138-140). This construction of the charter party is among the errors asserted on this appeal (see Specification of Error No. 1, *infra*).

The Court's alternative ground for holding Schnitzer liable for demurrage at the discharge port and unpaid freight was that Clause 8 of the charter party (stating

that inability of Amtro to exercise its lien on the cargo is a condition to Schnitzer's liability "should not be enforced on the record before me" (R. 144). This conclusion of the Court appears to be based upon three subsidiary holdings, all of which are challenged on this appeal (see Specifications of Error Nos. 5 through 11):

1. The implication (never expressly stated by the Court) that Amtro was unable to exercise its lien on the cargo because of congestion in the port of Tokyo (R. 142-144);

2. Amtro could not exercise a statutory lien under Japanese law on cargo while in the hands of consignees within two weeks after delivery, because delivery was to third parties (R. 144); and

3. Amtro was not in a position to assert its lien on the cargo because of representations of Schnitzer until December 7, 1961, that it would be responsible for the demurrage and unpaid freight (R. 140-142, 144).

The following background underlies this alternative holding of the Court.

When Amtro was unable to pay the monthly charter hire due to owners on November 7, 1961, it retained counsel to press its demands upon Schnitzer for immediate payment of or security for the demurrage accruing in Japan (Tr. 51-53, 103). Mr. Fletcher, Amtro's attorney, telegraphed Schnitzer on November 10, 1961 (Ex. 101) that Amtro would make arrangements to exercise the lien on the cargo under Clause 8 of the charter party, unless Schnitzer would guarantee full payment of

the demurrage at the discharge port and unpaid freight. Various negotiations and discussions ensued between Amtro and Schnitzer until December 7, 1961, when Schnitzer's counsel advised Mr. Fletcher to proceed with exercise of the lien, since Schnitzer was unwilling to assume liability for these amounts (Tr. 113-114; R. 141).

Meanwhile, Amtro and Owners had begun in November arrangements for exercise of the lien on the cargo of the NICTRIC (Tr. 110), to be handled through Owners' agents and attorneys in Tokyo, Dodwell & Co. and the McIvor firm, respectively. Dodwell & Co. sent letters to the Japanese consignees on November 27, 1961 (Ex. 113) notifying them of the Owners' instructions to exercise the lien on cargo unless accrued demurrage was paid immediately and further demurrage paid day by day. Dodwell cabled the Owners on December 9, 1961, advising that port congestion in Tokyo would complicate exercise of the lien, and recommended:

"THEREFORE IMMEDIATE LIENING ACTION INADVISABLE BEST WAIT UNTIL ABOUT 1500 TONS CARGO REMAINING IF LIEN STILL NECESSARY AT THAT TIME."
(Dep. Ex. F-4)²

This cable was sent six days after discharge of the 9,000 ton cargo had begun on December 3, 1961 (R. 105).

The only attempt found by the Court or shown by

² Depositions taken in Japan were offered in evidence at the trial as Exs. 44A through 44J, inclusive (Tr. 133-135). The offer presumably included the exhibits marked at the time of the depositions, and references to those exhibits are indicated as "Dep. Ex."

the evidence to have been taken to exercise the lien was Dodwell's inquiry to eight Tokyo stevedoring firms on December 12, 1961, about the availability of lighters, with replies that they could furnish none for this purpose (R. 142; Ex. 44E, p. 22; Ex. 44G, p. 160). There are 20 large stevedoring firms and some 50 smaller ones in the Tokyo harbor area (Ex. 44H, p 187-1) No attempt was made to secure lighters from other firms or at other times while the NICTRIC was in Tokyo harbor (Ex. 44E, p. 22, 126 Ex.; 44G, p. 163). No method for exercising the lien was considered or attempted by Amtro or Owners other than discharge into lighters (Ex. 44E, p. 136). No attempt was made to exercise the lien by stopping discharge and holding the cargo on board the vessel (Ex. 44E, p. 59; Ex. 44G, pp. 160, 168), or to inquire about partial discharge for lien purposes at a special 7-day berth (Ex. 44G, p. 168-169; Ex. 44H, p. 187-2, et seq.), or to explore any other means of exercising the lien.

It is Schnitzer's position on the appeal, as in the District Court, that there is no evidence to support the Court's finding that cargo was delivered to third parties, thus preventing exercise of the Japanese statutory lien on cargo in possession of the consignees (R. 144).

The Court found that Schnitzer had led Amtro to believe until December 7, 1961, that it would be responsible for the unloading demurrage and unpaid freight (R. 140-142). Apparently relying on this finding, the Court concluded that "Amtro was not in a position to effectively assert its lien on account of the representations of Schnitzer that the demurrage and unpaid freight would be paid" (R. 144). The total

cargo carried on this voyage was 8,991.142 long tons (Exs. 4-13). On the basis of the prices paid by the Japanese buyers for the cargo delivered to Tokyo, the cargo had an average value in Tokyo harbor of more than \$50 per long ton (see Exs. 16, 18-20, 109-112), and a total value of about \$500,000 (R. 196). Discharge of the cargo began on December 3, 1961, and was not completed until December 31, 1961 (R. 105). Thus, cargo having more than sufficient value to secure the demurrage and unpaid freight remained on board the vessel until the last week of December, 1961 (see Dep. Ex. B-19).³

Amtro at the trial offered the testimony of several witnesses by depositions taken in Japan in an attempt to show that congested port conditions rendered it unable to exercise its lien on the cargo for the demurrage and unpaid freight. This testimony was objected to by Schnitzer as hearsay and conclusion without factual foundation in the evidence. The Court finally determined that Schnitzer's objections should be made after the trial in writing, and apparently admitted the depositions subject to the post-trial objections (Tr. 133-139, 240-243). Although Schnitzer's objections were filed on November 30, 1964 (R. 123, et seq.), the Court failed to announce a ruling on them before its opinion and

³ Dep. Ex. B-19 was a cable from Dodwell to Owners on December 26, 1961 that 1200 tons remained on board on that date, and asking whether the lien was to be exercised. At \$50 per ton, that amount of cargo would have been worth about \$60,000. Owners replied that they were bringing suit against Schnitzer in Portland (which had been filed earlier on December 14, 1961), and instructed Dodwell:

"NEVERTHELESS ENDEAVOUR EXERCISE LIEN VIEW KEEPING VOYAGE CHARTERER RESPONSIBLE UNDER CLAUSE 8 VOYAGE CHARTER." (Dep. Ex. B-2)

findings were handed down on May 25, 1965 (R. 130, et seq.). The Court later on July 7, 1965, rendered a "nunc pro tunc" order (R. 184, et seq.) on Schnitzer's objections. The order in most instances fails to indicate clearly whether objections to particular deposition testimony were sustained or denied. For example, the ruling on Schnitzer's objections on hearsay grounds (R. 125-126) to eight specified portions of the deposition testimony of Amtro's witness Main was as follows (R. 185):

"Denies the motion to strike the entire testimony of the witness Main.

"Sustains the specific objections to certain of his testimony on the ground that it is hearsay or conclusionary; otherwise, the specific objections are denied."

Thus, it is most difficult to determine whether specific objections were sustained or denied. Since the Court's implied holding that Amtro could not exercise its lien on the cargo necessarily depends upon acceptance of some of the contested evidence in the Japanese depositions, it would appear that many of the specific objections were overruled. In any event, the failure to sustain a number of Schnitzer's objections to deposition testimony relating to attempted lien exercise is specified as error on this appeal (see Specifications of Error Nos. 12-17).

Questions on Appeal

Thus, the specifications of error on appeal deal with the following aspects of the Court's rulings and findings

underlying its decree holding Schnitzer liable for the demurrage and unpaid freight:

1. Whether the Court misconstrued the voyage charter party in holding that Clause 8 (the lien or cesser clause) was modified out of existence by Clause 18, so that there was no lien given on the cargo for demurrage and no condition of Amtro's inability to exercise the lien before Schnitzer could be liable (Specifications of Error Nos. 1-4).

2. Whether the Court erred in holding either that Amtro should not be held to the condition of exercising the lien or (by implication) that it had been unable to exercise the lien, within the meaning of the charter party cesser clause (Specifications of Error Nos. 5-9, 11).

3. Whether there was evidence supporting the Court's finding that cargo was delivered to third persons, not to consignees, thereby preventing exercise of the Japanese statutory lien upon the cargo in possession of the consignees (Specification of Error No. 10).

4. Whether the Court erred in admitting and relying upon certain evidence relating to the alleged inability to exercise the lien on the cargo (Specifications of Error Nos. 12-18).

5. Whether the Court misconstrued Clause 19 of the charter party in failing to exclude unused weekends and holidays throughout the demurrage period from computation of the demurrage, which accounted for \$12,483 of the total demurrage awarded against Schnitzer in the amount of \$5,757.10 (R. 105-106; Specification of Error No. 19).

Objections to the Court's findings and conclusions, as embodied in its opinion (R. 130 et seq.), were made by Schnitzer's motion for reconsideration and objections to findings (R. 155 et seq.). These were overruled by the Court (R. 182-183). Objections to admission of evidence in the form of deposition testimony were raised, as previously indicated, by post-trial motion (R. 123, et seq.) entered after the decree was filed.

SPECIFICATIONS OF ERROR—GROUP I

Construction of Charter Party

1. The Court erred in entering a decree (R. 153) against Schnitzer Steel Products Co. for any sum other than \$500 stevedore damage admittedly due (R. 106), in that the Court's conclusion that Clause 8 (cesser clause) was not a part of the charter party between Amtro and Schnitzer, was an erroneous construction of the charter party and based upon the erroneous findings of fact and conclusions of law specified below in Specifications of Error Nos. 2, 3 and 4.

2. The Court's finding and conclusion (R. 140) that Schnitzer was the author of the charter party and chargeable with its form, language, deletions and endorsements is unsupported by substantial evidence and clearly erroneous.

3. The Court's finding (R. 141) that Schnitzer's counsel took the position from November 17, 1961, until after completion of discharge of the cargo on December 31, 1961, that Amtro had no lien on the cargo for demurrage is unsupported by substantial evidence

and clearly erroneous, there being no evidence that Schnitzer's counsel ever took such a position.

4. The Court's finding and conclusion (R. 142) that all of Schnitzer's contracts for sale of the cargo (Exs. 16, 18, 20, 109, 110, 111 and 112), with one exception, provided that demurrage at the discharge port was for seller's (Schnitzer's) account is unsupported by evidence and a clearly erroneous construction of all the contracts, except the two contracts with Mitsui (Exs. 18 and 19).

SPECIFICATIONS OF ERROR—GROUP II

Failure to Exercise Lien on Cargo

5. The Court erred in entering a decree (R. 153) against Schnitzer for any sum other than the \$500 stevedore damage admittedly due (R. 106), since the Court erred in concluding (R. 144) that Clause 8 (ces-ser clause) of the charter party, requiring Amtro to exercise its lien on cargo for demurrage and unpaid freight as a condition to Schnitzer's liability therefor, should not be enforced against Amtro, said conclusion being based upon erroneous findings of fact and evidence erroneously admitted as specified below in Specifications of Error Nos. 6 through 18, inclusive.

6. The Court's finding (R. 142, 143) that exercise of the lien by holding the cargo on board the vessel would probably have caused the Japanese harbor authorities to move the vessel from its discharge berth and to prevent further discharge of cargo until after 50 to 100 other ships had discharged, is unsupported by substantial evidence and clearly erroneous.

7. The Court's findings (R. 143) that Schnitzer tried unsuccessfully to arrange for the discharge of the NICTRIC at "another [Harumi] wharf and that the lien could not have been exercised by discharge of cargo there is unsupported by substantial evidence and clearly erroneous.

8. The Court's finding and conclusion (R. 144) that Japanese port authorities would not have permitted the use of lighters for exercise of the lien on the cargo is unsupported by substantial evidence and clearly erroneous.

9. The Court's finding (R. 143-144) that no bonded storage space was available for exercise of the lien on cargo is unsupported by substantial evidence and clearly erroneous.

10. The Court's findings (R. 142-143, 144) that the consignees of the cargo had transferred title to the cargo to third persons and that third persons acquired possession of the cargo upon its discharge from the vessel, thus preventing exercise of the Japanese statutory lien, are unsupported by substantial evidence and clearly erroneous.

11. The Court's finding and conclusion (R. 144, 140-141) that Amtro was not in a position to assert effectively its statutory lien under Japanese law on the cargo, "on account of the representations of Schnitzer that the demurrage and unpaid freight would be paid," is unsupported by substantial evidence and clearly erroneous.

12. The Court erred in failing specifically to sustain Schnitzer's objections and motion to strike the fol-

lowing testimony by deposition (Ex. 44E) of Amtro's witness Saishoji:⁴

(a). Ex. 44E, p. 23, line 9 through the end of the page:

"Q. (by Mr. Fletcher) On the basis of your experience at that time, and knowledge, was there any time during December of 1961 when it would have been possible to obtain lighters with which to discharge this cargo from the vessel, other than discharge to the regular consignees?

A. No, I don't think so.

Q. Would it, on the basis of your knowledge and experience, and daily concern with the problem at that time, was there any time within December of 1961 where it would have been possible to obtain storage space for this cargo?

A. We tried similar actions on other ships, but at that time since September 1961 up to March of 1962, it was a very difficult time to arrange any lighters from shipping agent because even for the consignees themselves it was extremely difficult to get lighters for their own cargo, and we are not customers for the lighter owners and also we are not customers for the stevedoring companies in Tokyo because we only handled quite a lot of trampships and free-out terms, therefore the stevedores concerned usually they gave priority in giving lighters to their own customers. That is why I don't think we could get any lighters from stevedoring companies in Tokyo at that time, even in January or February next year—1962, I mean."

⁴ The page and line references in all the following specifications refer to the specific material subject to the motion or objection. Material preceding or included in the following quotations for the purpose of understanding the testimony and objection, but not subject to the motion to strike or objection, is in brackets.

(b). Ex. 44E, p. 24, lines 6-10, and line 23 through p. 25, line 4:

“[Q. (by Mr. Fletcher) You mentioned early in your testimony the fact that you could not get bonded warehouse space in which to put this scrap. Why was bonded warehouse space necessary?]

A. If, in order to exercise lien on the cargo, owners must discharge cargo into bonded warehouse or shed, because the cargo was imported from abroad and Customs Office do not allow discharge any other place.

[Mr. Lewis: Just for the record, I would like to make objection here that this entire line of testimony is irrelevant to the issues in the case, and constitutes opinion evidence.]

.

[Q. (by Mr. Fletcher) I notice that, Mr. Sai-shoji, that in your Exhibit F-4, you advised owners that the action of ceasing discharge and holding the cargo in the ship would result in port authorities' ordering 'Nictic' out of berth, necessitating awaiting turn later for reallocation of the berth. What was the basis of your information on that subject?]

A. When ship came in at Tokyo for discharge of scrap cargo, I think that Tokyo Harbour authorities nominated 5 or 6 berths for discharge of scrap cargo, and so many ships with scrap cargo waiting for berth outside the Harbour, in order of ship's arrival, so the berth was assigned to the ship in order of the time of ship's arrival in Tokyo, so when any berth was nominated to a ship she had to discharge her cargo as soon as possible to vacate berth for other ships which were waiting for berth. So if we cease discharge in the Harbour, then the Port authorities do not agree to keep the

ship in Harbour. And maybe they requested the ship to go outside Harbour to wait further allocation of the berth."

(c). Ex. 44E, p. 57, lines 29-33:

"[Q. (by Mr. Lewis) That if the ship had stopped discharge it would have lost berth. That's merely your opinion.]

A. No, that was advised by the Port authorities—for example, if we don't work two days here inside the harbour, harbour authority give instructions why no work here, and similar stoppage happened in Yokohama and they actually—ship was ordered to go outside."

(d). Ex. 44E, p. 34A, line 3 through p. 35, line 17:

"Q. (by Mr. Fletcher) Mr. Saishoji, as a practical matter, would it have been possible to seize and stop delivery of the cargo while it was in the lighters which took the cargo from the vessel to wherever it was going? That is, to stop the lighters and make them hold the cargo instead of delivering.

A. No, I don't think so, because the lighter-owners, they let the lighters hire to the others on the basis of lighterage that cargo was to be discharged as soon as possible and if we request exercise lien on the cargo in the lighters they only get a small amount of demurrage per day instead of the rate of lighters. So, the lighterowners, usually they don't agree in such circumstances of acute shortage of lighters in port.

Q. Under the condition at that time with the acute shortage of lighters, would the harbour authorities have let you do something like that, that is, tie-up a set of lighters for a while?

Mr. Lewis: I would like to register a contin-

uing objection.

A. I don't think so."

- (e). Ex. 44E, p. 65, lines 10 through 24, and p. 66, lines 1 through 10 and 16 through 31:

[Q. (by Mr. Fletcher) To earlier this year in the summer or early fall, did you, at that time, inquire of the various consignees of the cargo of the 'Nictic' what the terms were on which they have sold the cargo to the steel mills?

[A. You mean when?

[Q. Well, did you, at any time, in, ah, inquire of the consignees, ah, no strike that. Did you at any time, this year, not 1961, this year, inquire of the consignees what terms they, they had sold the cargo to their ultimate consumers on?

[A. Yes, I have asked.

[Q. When were those inquiries made?

[A. I think I have . . .

[Q. Approximately, it doesn't matter exactly.

[A. That August, I think.]

Q. I see. And what did the consignees tell you at that time?

A. They told us that the cargo, their cargo was already sold to consumers and the details of the, their contracts they don't give us, but usually when they purchase a cargo from abroad . . .

Mr. Lewis: I object to anything now.

A. . . also make contract with the consumers.

Q. Apart from, I'm not interested now in the price and other details, but did they tell you the delivery terms on their contracts with their consumers?

A. They said some of consignees, their cargo delivery upon ship's arrival on board on 'Nictic.'

.

[Q. Well, now, Mitsui said, when you asked Mitsui about this, what did they tell you about delivery terms on which they had sold the cargo to the steel mills?]

A. Some lot of the cargo was sold to their consumers from discharge on discharge from 'Nictic' to lighters and some cargo on board lighters. I think two items they mentioned.

Q. So that some of it was on the discharge into the lighters, and the other part was on the lighters.

A. Yes.

Q. Was the place where delivery was to be made to their customers.

A. Yes.

.

[Q. In the case of Toyo Menka, what did Toyo Menka tell you?]

A. They also sold the cargo to the customers, consumers, but they don't mention exactly the date of delivery, and place of delivery, but they said, only they said the cargo was sold to the consumers.

Q. Did they say whether or not the cargo had been sold by the time the vessel arrived?

A. Yes, they said already sold.

Q. Now, in the case of Okaya & Co., what did they tell you?

A. I remember that the cargo was already sold to the consumers but they don't mention the details.

Q. And in the case of Nomura Trading Company, what did they tell you?

A. When I checked the consignees, 7 consignees they all replied cargo was already sold to the consumers. So, the same reply."

As directed by the Court (Tr. 136-137, 240), Schnit-

zer's objections to the foregoing testimony were by written motion, as follows (R. 123, 124-125):

"III

"Moves to strike the entire testimony of Kimitoshi Saishoji relating to demurrage and attempts to exercise the lien except for his contact with stevedores for the reason that the witness himself testified that he had no personal knowledge. (See p. 124, line 21 through p. 130, line 10; p. 134, lines 14-19, p. 135, lines 14-16).

"If the motion to strike the entire testimony other than his testimony relating to contact with stevedore companies is denied. Schnitzer moves to strike the following portions of testimony upon those grounds and/or that the best evidence was not offered:

.

P. 24, line 23 through p. 25, line 4.

P. 23, line 8 through end of page.

P. 34A, line 3, through p. 35, line 17, for the additional reason that the testimony is speculative and opinion evidence which is not admissible upon questions of fact.

.

P. 24, lines 6-10.

.

P. 57, lines 29-33, hearsay, opinion and supposition.

P. 65, lines 10-24.

P. 66, lines 1-10, 16-31."

The Court's ruling on these objections was by nunc pro tunc order (R. 184 et seq.) after its opinion was rendered, as follows:

"III

"Denies the motion to strike the entire testimony of the witness Kimitoshi Saishoji, for the reason that some of the testimony is relevant and material to the issues in the case.

"Sustains the specific objections to the testimony of said witness on the ground that the same was hearsay or opinion evidence; otherwise, the specific objections are overruled."

13. The Court erred in failing specifically to sustain Schnitzer's objection and motion to strike the following testimony by deposition (Ex. 44F) of Amtro's witness F. A. L. Morgan:

Ex. 44F, p. 77, lines 11 through 21:

"Q. (by Mr. Fletcher) About December 8, did you inquire concerning obtaining lighters, space, etc., for exercising lien on cargo?

A. Yes. In the company of principal of John Manners, we interviewed stevedore representative in Tokyo area, and as inquiries were made at that time, we understood that was a very great shortage of lighters which normally are required for scrap and that it was almost impossible to find storage arrangements on shore and that it would be unfeasible under most circumstances to exercise lien—this was the opinion of the stevedore."

Schnitzer's objection was by written motion (R. 125) as follows:

"IV

"Moves to strike the entire testimony of F. A. L. Morgan on the subjects of demurrage and attempts to exercise a lien on the ground that by the

testimony of the witness himself he did nothing, except for talks with stevedores, to exercise a lien on the cargo. (See p. 152-3, lines 16-23).

"Moves to strike the following based on hearsay and speculation:

.

"P. 77, lines 11-21 and on the additional ground that the answer constitutes the opinion of a third party as stated by the witness himself."

The Court's ruling was by nunc pro tunc order as follows (R. 185):

"IV

"Denies the motion to strike the testimony of the witness F. A. L. Morgan.

"Sustains the specific objections on the ground of hearsay or where the same may be opinion evidence; otherwise, the specific objections are denied."

14. The Court erred in failing to sustain Schnitzer's objection to Deposition Ex. B-11, a letter dated January 19, 1962, from Amtro's agent F. A. L. Morgan to Amtro's manager Stewart stating, inter alia, that Schnitzer's Tokyo representative had unsuccessfully attempted to arrange for discharge of the NICTRIC out of turn at a special quick discharge berth.

Schnitzer's objection was by written motion as follows (R. 127-128):

"VIII

"Schnitzer objects to the following documentary evidence appended to the depositions taken in Japan upon the ground that said exhibits are incom-

petent, irrelevant and immaterial, constitute hearsay and are not binding on Schnitzer:

"B-11 (consisting of three pages)."

The Court's ruling was by nunc pro tunc order as follows (R. 186):

"VIII

"Overrules the objections to the introduction of Exhibits F-23 and B-11, the former being part of a record kept in the usual course of business and the latter having general background relevancy."

15. The Court erred in failing to sustain Schnitzer's objection to Deposition Ex. F-23, a newsletter of Pacific Marine Corporation, which is described in the Court's opinion at R. 143 as refuting the availability of bonded storage space in Japan for exercise of the lien on cargo.

Schnitzer's objection was by written motion (R. 127-128) as follows:

"VIII

"Schnitzer objects to the following documentary evidence appended to the depositions taken in Japan upon the ground that said exhibits are incompetent, irrelevant and immaterial, constitute hearsay and are not binding on Schnitzer:

F-23 (consisting of seven pages)."

The Court's ruling was by nunc pro tunc order as follows (R. 186):

"VIII

"Overrules the objections to the introduction of Exhibits F-23 and B-11, the former being part of a record kept in the usual course of business and the latter having general background relevancy."

16. The Court erred in failing specifically to sustain Schnitzer's objections and motion to strike the following testimony by deposition (Ex. 44G) of Amtro's witness Main:

(a). Ex. 44G, p. 160, line 21 through the end of the page:

"[Q. (by Mr. Baillie) What about attempting to retain cargo in the ships in order to exert a lien? Could that have been done?]

A. The only way of retaining the cargo in the ships is to cease discharging, which meant, at that time, that the ship risked the extreme probability of being moved away, in fact, we were told by the port authorities at a number of ports in Japan, that the ships would be moved out of berth and sent to anchor outside and when the ships would be brought back was a matter of conjecture, they would quite easily have to wait their turn and there were bigger ships waiting to come in to discharge."

(b). Ex. 44G, p. 161, lines 6-9:

"Q. (by Mr. Baillie) Oh, I should have asked you before, as a general question, were you ever able to impress a lien upon the cargo of the 'Nictic'?

A. On the 'Nictic', no."

(c). Ex. 44G, p. 173, lines 27-29:

"[Q. (by Mr. Lewis) Well, let me ask you, how do you go about liening a cargo after discharge?

[A. Is it relevant if this is not possible.

[Q. Yes certainly. I want to know why you say it's not possible.]

A. Well, I say it was not possible because there

was no storage space ashore, and, nor could we get barges to hold it in the barges or the lighters."

(d). Ex. 44G, p. 177-3, line 9 through p. 177-4, line 18:

"Q. (by Mr. Fletcher) Mr. Main, I take it there was, the harbor authorities in the Tokyo area were interested in relieving congestion as quick as possible, is that correct, according to your acquaintance and experience in these things?

A. Yes.

Q. And one of the main sources of congestion was shortage of lighters?

A. Yes.

Q. On the basis of your general acquaintance with the situation then, do you believe that the harbor authorities would have allowed anyone to tie up lighters for a period of several days for the purpose of liening cargo while in the lighters and holding them in the lighters for that purpose?

Mr. Lewis: I object to that question.

A. We ascertained on a number of occasions and in a number of ports in Japan that the authorities will not permit lighters to be tied up.

Q. Now Mr. Main this. You previously stated that you had ascertained that the port authorities would, would take a vessel out of berth and make her go back to the end of the line if she stopped discharging. To your knowledge and on the basis of your acquaintance, with conditions then, was this just as true when she only had 1500 tons more to discharge as when, as in the beginning? Did it make any difference when in the discharge this occurred?

A. Not as far as we were aware. We were given to understand that throughout this job, that still applied.

Mr. Lewis: What still applied?

A. The ship, if she ceased discharging would be moved out of the berth in order to make way for another ship to be discharged.

Q. Now, these special berths for quick seven day discharge Mr. Lewis was asking about, were these berths on which one would not be allowed to store cargo or store the cargo for any length of time?

Mr. Lewis: Ask him if knows, if you know.

A. I don't know definitely. I can only say this is extremely doubtful cargo would be permitted to lie alongside on the pier. I don't think any cargo is allowed to lie on the pier for a long period.

Mr. Lewis: I object to all of that, everything.

Q. Well, was there at this time a shortage of custom warehouse facilities in which to place the cargo?

Mr. Lewis: Please define customs warehouse areas.

Q. Any area which would be proper, which the Japanese authorities would consider proper and possible, within which to put cargo, pending its delivery to consignees who cleared it through customs.

A. Yes, it was a definite fact that at that time that the facilities were not available for the cargo to be held for a lien."

(e). Ex. 44G, p. 177-6, lines 9 through 19:

"Q. (by Mr. Baillie) Mr. Main, when you say a vessel might be sent out by the officials in charge, out of berth, again to wait her turn, she would take her turn with the last vessel arriving in port, would she not? After the last vessel arriving in port, isn't that what is meant by sending her out of berth to . . .

A. Yes. To take her turn with the ships then lined up outside.

Q. And she would follow the last one in line.

A. She'd be the last in line.

Q. And of course you did have knowledge of when the last ship came into port, did you not?

A. Yes. We had knowledge of when the last ship came into port and we continually had knowledge of the prospects of waiting for that last ship."

Schnitzer's objections were by written motion, as follows (R. 125-126):

"V

"Moves to strike the entire testimony of Main relating to demurrage and attempts to exercise a lien on the cargo, except for testimony relating to a November 27th letter to the consignees for the reason that by the witness' own testimony he personally did nothing to lien the cargo (see p. 162, line 30, p. 163, lines 17-18, p. 172, lines 19-24) and that he could not recall what he personally had to do with attempts to lien the cargo. (See p. 162, lines 7-10)

"Moves specifically to strike the following:

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"P. 160, lnes 21 through end of page on the ground that it is hearsay.

"P. 161, lines 6-9, on the ground that the alleged testimony is a conclusion, and the witness testified that he personally did not do anything to exercise a lien. (See p. 162, line 30, p. 163, lines 17-18, p. 172, lines 19-24).

"P. 173, lines 27-29, on the ground of hearsay. (See p. 174, lines 3-10).

"P. 177-3, line 9 through 177-4, line 18, on the grounds of no personal knowledge, the answers constitute hearsay evidence, and are at best statements of conclusions.

"P. 177-6, lines 9-19, on the ground that the evidence is speculative and hearsay."

The Court's ruling was by nunc pro tunc order, as follows (R. 185):

"V

'Denies the motion to strike the entire testimony of the witness Main.

"Sustains the specific objections to certain of his testimony on the ground that it is hearsay or conclusionary; otherwise, the specific objections are denied."

17. The Court erred in failing specifically to sustain Schnitzer's objections and motion to strike the following testimony by deposition (Ex. 47) of Owner's witness, Captain Cassimatis:

(a). Ex. 47, p. 19, line 23 through p. 20, line 9:

"Q. (by Mr. Tatum) And were you able to exercise a lien on the cargo of the NICTRIC?

A. No.

Q. Why not?

A. Because according to the advice available which was the best advice at the time for me, which was namely McIver and Dodwell, it was impossible to do that sort of thing in Japan.

Q. Why was it impossible?

A. Why, I couldn't tell you definitely. The idea was that the congestion was terrific. There were no lighters, there was no warehousing, there was no

space where to put this cargo, and the thing was simply not feasible."

- (b). Ex. 47, p. 44, line 25 through p. 45, line 9, and p. 45, lines 20-22:

"[Q. (by Mr. Lewis) You didn't know what efforts were being made at that time by Mr. Main?]

A. What I know, I know that I went myself with Main twice at McIver's and once alone, and I was pushing along all the time seeing what we could do about leaving [sic] the cargo, and then both McIvors and Main told me, 'Sorry, old boy, we cannot do anything about leaving [sic] the cargo, for the simple reason that this cargo has been sold on different terms than the ordinary terms.' It has been sold on, whatever you say, CQ—

Q. CQD?

A. CQD. And of course we have no handle . . . but according to what both Dodwell and McIver told me, they couldn't leave [sic] the cargo because there was no handle to press this."

- (c). Ex. 47, p. 51, lines 6-9:

"A. (by Captain Cassimatis, on cross-examination) . . . But what I am a hundred per cent sure, from the advice of the Club, which was McIver, and advice of Dodwell, which is Main, but perhaps his general manager behind him, was that there was no chance of liening the cargo."

- (d). Ex. 47, p. 59, line 23 through p. 60, line 13:

"Q. (by Mr. Tatum) Now, in this instance of the NICTRIC, to clear up this advice from McIver and Dodwell, did they advise you that under the terms of the voyage charter and the contracts, you had no claim against the receivers for demurrage?

A. That's so, that is correct.

Q. Now, that's one claim that you received advice on. Now, did they likewise advise you that you had no right to lien the cargo because of the shortage of facilities?

A. That is correct.

Q. So those were the two pieces of advice that they gave you?

A. Which to me was sufficient at the time, because it was the best thing I could get.

Q. And that was advice from the Club's lawyer, McIver, in Tokyo?

A. That's right.

Q. And advice from Dodwell & Company?

A. That is correct."

Schnitzer's objection was by written motion as follows (R. 127):

"VII

'Moves to strike the testimony of G. Cassimatis in the following particulars:

"P. 19, line 23 to p. 20, line 9, on the ground that the witness had no personal knowledge, that his testimony is based on hearsay and expresses opinions and conclusions on matters depending on facts in issue. (See p. 43, line 24 to p. 44, line 17, p. 54, lines 7-11).

"P. 44, line 25 through p. 45, line 9, 20-22, on the ground that the testimony is hearsay, speculative, non-responsive, and tends to prove no issue in the case.

"P. 51, lines 6-9, on the ground that the testimony is hearsay and non-responsive.

.

'P. 59, line 23 through p. 60, line 13, on the ground that the testimony is hearsay."

The Court's ruling was by nunc pro tunc order as follows (R. 185-186; see also Tr. 18-25):

"VII

"Sustains the objections to the testimony of the witness G. Cassimatis insofar as the same is hearsay and conclusionary."

18. The Court erred in failing to sustain Schnitzer's objections to discharge reports, Exhibits 26, 27 and 23, as follows (Tr. 10-12):

"MR. TATUM: Now, if your Honor please, I would like to offer . . . Exhibit 26, which is the discharge report in Tokyo for one of the Mitsui contracts, and No. 27, which is likewise a certificate of discharge for the other Mitsui shipment in Tokyo. Also, Exhibit 23, which is the discharge survey report for a shipment to the Iwai company.

THE COURT: Any objection?

MR. KRAUSE: Your Honor, could we have a statement as to the purpose of this offer?

THE COURT: All right. Make your statement . . . , Mr. Tatum.

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THE COURT: And No. 26?

MR. TATUM: Exhibit 26 is the discharge report showing the surveyors in Japan who surveyed and measured these turnings. It shows the delivery was on behalf of Mitsui, but it shows what was delivered and where. It relates to Mr. Krause's claim that we could have exercised a lien in the hands of Mitsui. This proves it was never delivered to Mitsui.

THE COURT: And 27?

MR. TATUM: The same is true of 27 and the same is true of 23.

THE COURT: All right, Mr. Krause.

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MR. KRAUSE: May I say one word about the last one of these exhibits?

THE COURT: That would be 26, 27 and 23.

MR. KRAUSE: Those reports do not show that the cargo was not delivered to Mitsui. I mean, you can't take a report of that sort and by that prove that the cargo went into the hands of an innocent purchaser for value.

THE COURT: Mr. Krause, I believe that is a question of argument as to the interpretation of the instrument itself. They will be admitted."

SPECIFICATIONS OF ERROR—GROUP III

Erroneous Calculation of Demurrage

19. The Court erred in failing to exclude from the amount of demurrage awarded against Schnitzer the sum of \$12,483 (see R. 105-106) for demurrage charges attributable to weekends and holidays after lay time had expired, by erroneously construing (R. 144-145) Clause 19 as applicable only to the laytime period, and not to the demurrage period after the expiration of the laydays.

SUMMARY OF ARGUMENT

1. Clause 8 (lien or cesser clause) of the voyage charter party defines the liabilities of the parties for demurrage, and was not modified by Clause 7 or 18 of the charter party.

2. Since the charter party, including Clause 8, was

incorporated in the bills of lading, the receivers of the cargo were liable for the unloading demurrage and unpaid freight, and Schnitzer was liable only to the extent that Amtro was unable to exercise its lien on the cargo for these sums.

3. Amtro failed to exercise the lien, and there is no substantial evidence of any real or good-faith effort by Amtro or Owners to do so; the condition to Schnitzer's liability was therefore not met.

4. If Schnitzer was liable for the demurrage and unpaid freight, Clause 19 provides that demurrage was not to run on weekends and holidays, and the amount recoverable against Schnitzer was \$12,483 less than the \$57,757.10 awarded by the Court.

ARGUMENT

I

The District Court erred in construing the voyage charter party to the effect that Clause 8 (lien or cesser clause) was inoperative.

(Specifications of Error Nos. 1-4)

Clause 8, the lien or cesser clause, of the voyage charter party (Ex. 2) between Amtro and Schnitzer provided:

"8. Owner shall have a lien on the cargo for freight, dead-freight, demurrage. Charterers shall remain responsible for dead-freight and demurrage incurred at the port of loading. Charterers shall also remain responsible for freight, and demurrage incurred at port of discharge, but only to such extent as the Owners have been unable to obtain payment thereof by exercising the lien on the cargo." (Emphasis supplied)

Under this clause, the liability of Schnitzer for unpaid freight and demurrage at the discharge port was only secondary, conditioned upon Amtro being unable to obtain payment from the receivers of the cargo by exercise of its lien.

The District Court held (R. 138-142) that the ceser clause and its limitation upon Schnitzer's liability was ineffective, because modified by Clauses 7 and 18, which the Court interpreted standing alone as imposing unconditional liability for unloading demurrage and unpaid freight upon Schnitzer. Clause 7 provided:

"7. Demurrage, if incurred, to be paid by Charterers at the rate of Seven Hundred Dollars (\$700) per day or pro rata for any part of a day."

Clause 18 provided:

"18. Cargo is to be loaded stowed and discharged within a total of twenty-three (23) weather working days of 24 hours. Sundays and holidays excepted unless used, in which case actual time used to count. If longer detained, Charterers to pay demurrage at the rate stipulated in Clause 7 and payment is to be made in the same currency as freight payment . . . "

The Court reached this interpretation of the charter party on four grounds:

1. Clause 18 was an addition to the original printed form of the charter party (R. 138-139);

2. Schnitzer was the author of the charter party and chargeable with its form, language, deletions and endorsements (R. 140);

3. Schnitzer agreed with the Court's interpretation of the charter party until December 7, 1961, when Schnitzer denied responsibility for the sums in dispute (R. 140-142); and

4. Schnitzer's contracts for sale of the cargo to its Japanese consignees provided, with one exception, that demurrage at the discharge port was for seller's (Schnitzer's) account (R. 142).

Schnitzer submits that the first of these grounds is irrelevant, since Clause 18 does not conflict with Clause 8, and that the second, third and fourth grounds, as well as the Court's overall construction of the charter party provisions on liability for demurrage and unpaid freight, are erroneous.

Cesser Clause-Historical Background

A correct interpretation of Clause 8 and the charter-party provisions on unloading demurrage should take into account the historical use of the cesser clause in charter parties.

Vessels engaging in international trade have traditionally sailed under charter parties containing a cesser clause (Tr. 156), usually in substantially the following terms:

"Charterers' responsibility to cease when cargo is all on board and bills of lading signed, but master or owners to have an absolute lien on cargo for freight, deadfreight and demurrage."⁵

The cesser clause, when the charter party terms are

⁵ Quoted from the charter party construed in *The Hans Maersk*, 266 Fed. 806, 808 (CCA 2, 1920).

incorporated in the bills of lading, is construed to impose liability upon the receivers of the cargo for demurrage and unpaid freight at the unloading port. Charterer's liability ceases upon loading of the cargo, except to the extent that the lien given to the vessel covers less than ("are not commensurate with") the liability which it is intended to secure. This is well-settled law under the standard cesser clause. See, e.g., *Yone Suzuki v. Central Argentine Railway*, 27 F.2d 795 (C.C.A. 2, 1928), cert. den. 278 U.S. 652; *The Hans Maersk*, 266 Fed. 806 (C.C.A. 2, 1920); *Crossman v. Burrill*, 179 U.S. 100, 45 L. Ed. 106, 21 S. Ct. 38 (1900); Tiberg, *THE CLAIM FOR DEMURRAGE* (1962), pp. 15 *et seq.*⁶

The basic printed voyage charter party in this case (Exs. 2, 75) is the GENCON form which has been in use since 1922, and is commonly employed for scrap cargoes (Ex. 79, p. 29; Tr. 177, 198). Its cesser or lien clause (Clause 8), when the charter party is incorporated in the bills of lading, creates substantially the same liabilities for demurrage as the more common cesser clause in other charter party forms: demurrage at the discharge port becomes the liability of the receivers of the cargo, and the charterer remains responsible for it only to the extent that the lien given to the vessel cannot be exercised against the cargo. Compare the similar interpretations and results under the two

⁶ This excellent work totaling 95 pages by Swedish Professor Hugo Tiberg is published by Stevens & Sons, Ltd. of London. It deals succinctly, but with citations to and discussions of the legal authorities, with demurrage law of the United States, as well as of other maritime countries. It is the most helpful work on demurrage that we have been able to find.

forms of cesser clause in *The Arizpa*, 63 F.2d 42; (C.C.A. 4, 1933), cert. den. 290 U.S. 648, and *The Luossa*, 1936 A.M.C. 213 (Arb., 1935).

Thus, the legal effect of the cesser clause, both in its more common form and in the GENCON form, and its incorporation into the bills of lading, is to allocate liability for unpaid freight and demurrage at the discharge port to the receivers of the cargo, and to charge the vessel with the duty of collecting it from them by exercise of the lien. Only if the lien cannot be exercised, so that the vessel's remedy becomes illusory, does the charterer remain liable for such amounts. This doctrine soundly recognizes that receivers of cargo under the usual sale contracts and bills of lading have the power to and do control the discharge of the vessel. See *The Hartismere*, 1937 A.M.C. 594, 598, 18 F. Supp. 767 (D. Md. 1937). This allocation of unloading demurrage liability created by the cesser clause and its incorporation into the bills of lading places incentive on those responsible for discharge to accomplish it with a minimum of delay.

Thus, the requirement that the vessel exercise its lien for demurrage on cargo of the receivers is not merely a *pro forma* condition to holding the charterer responsible, but an agreement of the vessel to collect unloading demurrage and unpaid freight from the consignees, the parties primarily liable for it, at a time when the pressure is greatest upon them to meet that liability. If the ship fails to require the receivers to pay the demurrage at this time, the complexities arising from the location of the shipper and buyers in different

countries with variant legal systems may make it difficult or impossible for the charterer-shipper to enforce the buyers' ultimate liability for the demurrage.

Changes in Original Printed Form Do Not Alter Operation of the Cesser Clause

The District Court held that Clause 18, added to the original printed form, and the alteration of the original printed form of Clause 7 of the voyage charter party conflicted with and modified the allocation of liabilities of the cesser clause (R. 138-140). The Court's construction of the charter party is, we submit, plainly erroneous.

The Court found conflict in Clauses 7 and 18 with Clause 8 by quoting only a portion of two sentences in the first two of those clauses, thus destroying their context: "demurrage, if incurred, to be paid by Charterers" (from Clause 7); "Charterers to pay demurrage at the rates stipulated in Clause 7" (from Clause 18). Referring to its quotation of these two portions of sentences from Clauses 7 and 18, the Court stated:

"Thus, in the typewritten provisions, the charterer has not only once, but twice, made *an unqualified promise* to pay the demurrage." (R. 139, lines 9-11, emphasis supplied; see also R. 140, lines 2-4.)

By placing periods after the portions of Clauses 7 and 18 which the Court referred to, they were taken out of context. The entire sentence of Clause 7, quoted only in part by the Court, reads:

"Demurrage, if incurred, to be paid by Charterers at the rate of Seven-Hundred Dollars (\$700) per day or pro rata for any part of a day."

The function of Clause 7 is not to allocate liability for demurrage, but to agree upon the rate at which demurrage would be paid. The same was true of the original printed language of the GENCON form, which also specified the number of laydays before demurrage would begin to accrue. See Ex. 75, Clause 7.⁷ Clause 7 as modified in the NICTRIC charter party also recognizes, as do Clauses 8, 16, 17, 18 and others, that the voyage charterer—as between it and Amtro—was to control and to be responsible for arrangements for loading and discharge of the vessel.

Clause 8 of the charter party then goes on to define the liabilities of the parties for demurrage, giving Owners a lien on the cargo and stating that Charterers are to remain responsible, notwithstanding the lien, for demurrage incurred at the *loading* port; but Charterers are to be responsible for unpaid freight and demurrage at the *unloading* port

“only to such extent as the Owners have been unable to obtain payment thereof by exercising the lien on the cargo.”

Clause 18, among many additions in the NICTRIC charter party to the original printed GENCON form, modifies and expands upon Clause 7, not Clause 8. It specifies the number of days within which cargo is to be loaded, stowed and discharged, how those days are to

⁷ Clause 7 in the original printed GENCON form (Ex. 76), before any deletion or additions, read:

“Ten running days on demurrage at the rate of \$ per day or pro rata for any part of a day, payable day by day, to be allowed merchants altogether at ports of loading and discharging.”

be calculated, and refers to Clause 7 for the rate at which demurrage is to be paid.

Thus, Clause 18, like Clause 7, contains provisions relating to demurrage, wherever incurred, and does not modify the allocation of liability for demurrage set forth in Clause 8. The conflict with Clause 8 found by the Court in Clauses 7 and 18 on liability for demurrage (R. 138-140) plainly does not exist. The Court found conflict with Clause 8 by reading only parts of sentences in Clauses 7 and 18, overlooking the remainder of each sentence and the function of both clauses in the charter as a whole. The Court plainly erred in reading Clauses 7 and 18 as containing "specific language under which Schnitzer, without qualification, agrees to pay the [unloading] demurrage" (R. 140, lines 2-4).

The only two cases we have found on the cesser clause in the GENCON form of charter party are "*Z*" *Steamship Co., Ltd., v. Amtorg, New York*, 61 Lloyd's List L. R. 97, (K. B. Div. 1938), and *The Luossa*, 1936 A.M.C. 213 (Arb. 1935). Both cases illustrate the function of the cesser clause in defining liability of the parties for demurrage and its harmony with other clauses dealing with the rate at which demurrage is to be paid and the method of its calculation. Like Amtorg here, the vessel owner in *The Luossa* argued that an addition to the original printed form of the GENCON charter modified the cesser clause. As the arbitrators stated in that case (1936 A.M.C. at 216-217), the parties would have stricken out Clause 8, if they had not intended it to be given effect along with other clauses in the charter party, including those added to the original printed form.

**No Evidence Schnitzer Author
of Charter Party**

The Court, finding conflict in Clauses 7 and 18 with Clause 8, resolved it against Schnitzer, as author of the charter party (R. 140). There is no evidence that Schnitzer authored the language of the changes and additions to the original printed GENCON form. The evidence is that Schnitzer turned over to Seacharter Company, a charter broker, a charter previously used for a scrap cargo carried on the vessel KEHREA, as a sample for discussion (Tr. 177). The provisions of the KEHREA charter party pertaining to demurrage, including the deletions from and additions to the original printed language in Clauses 7 and 8, and the addition of Clause 18, were substantially identical to the charter party finally agreed upon for the NICTRIC, except that in the NICTRIC charter Sundays and holidays were to count, if used (Ex.. 76, 2; Tr. 200, 36, 42).

All Schnitzer did was offer as a sample for discussion with Amtro a charter party which had been used in a prior scrap cargo. There is no evidence as to which of the parties to the KEHREA charter, if either of them, made the changes from the original printed GENCON form, and no evidence that Schnitzer or Amtro drafted the modifications of the KEHREA charter which appear in the NICTRIC voyage charter.

**No Evidence Schnitzer Agreed With Court's
Construction of Voyage Charter**

The Court, attempting to buttress its interpretation that Clause 8 had been, in effect, modified out of the charter party, found that Schnitzer and its counsel took

the position until December 7, 1961, "that in fact there was no lien on the cargo," and that until that date Schnitzer interpreted the contract 'in line with Amtro's and this Court's conclusions" (R. 141, lines 5-14, 20-22). This finding is without any evidentiary support and clearly erroneous.

The record shows that all parties assumed the existence of the vessel's lien on the cargo until after this case was filed, and that Amtro repeatedly notified Schnitzer of its intent to exercise the lien.

The pleadings of Owners and Amtro alleged Clause 8 of the voyage charter party and that Owners and Amtro were unable to exercise the lien on cargo because of port congestion. Owners' original libel filed on December 14, 1961, while the cargo was being discharged from the NICTRIC, pleaded Clause 8 of the voyage charter party verbatim and alleged in Article XV (R. 4):

"Because of the congested port conditions at the Port of Tokyo, Owners have been unable to obtain payment of the demurrage monies earned on the said voyage by exercising a lien on cargo, although they have made diligent efforts to effect the same."

The amended libel, filed almost a year later on November 7, 1962, contained the same allegations (R. 39). Amtro's cross-libel against Schnitzer filed on January 31, 1962, contained identical allegations (R. 18). Owners continued to assert the existence of a lien under Clause 8 and their inability to exercise it, as satisfaction of the condition upon Schnitzer's liability, as late as the filing of the Pretrial Order on July 20, 1964 (R. 108, Para. 8

and 9). By this time, however, Amtro was claiming that Clause 8 of the voyage charter party was ineffective and that Amtro had no obligation "to endeavor first to obtain payment of freight and demurrage by exercising the lien on the cargo" (R. 109, Para. 3).

The first demand by Amtro's counsel upon Schnitzer for payment of the demurrage accruing in Japan was Mr. Fletcher's telegram of November 10, 1961, to Leonard Schnitzer (Ex. 101, Tr. 103), which read:

"WE REPRESENT AMTRO CORP. RE SS NIC-
TRIC. AMTRO NOW FORCED MAKE AR-
RANGEMENTS EXERCISE LIEN ON CARGO
UNDER CLAUSE 8 CHARTER UNLESS YOU
ADEQUATELY SECURE PAYMENT DEMUR-
RAGE. AS YOU KNOW EXERCISE LIEN IN
JAPAN OR TAKING CARGO ELSEWHERE
WILL CAUSE GREAT EXPENSE AND AD-
DITIONAL DELAY OF VESSEL WHICH WILL
GO TO REDUCE PROCEEDS OF LIEN EXER-
CISE AND ADD TO YOUR LIABILITY FOR
DEFICIENCY UNDER CHARTER. TO AVOID
THIS AMTRO PREPARED TO PERMIT DIS-
CHARGE OF CARGO TO RECEIVERS WITH-
OUT EXERCISING LIEN ON CONDITION
YOU AGREE FIRST GUARANTEE FULL PAY-
MENT FREIGHT AND DEMURRAGE DUE
UNDER CHARTER WITHOUT AMTRO EX-
ERCISING LIEN."

Mr. Fletcher's letter of November 14 to Schnitzer (Ex. 115) offered to waive Amtro's lien against the cargo under Clause 8, if Schnitzer would agree to be responsible for the demurrage and unpaid freight.

Attached to the letter was Mr. Fletcher's draft of a

proposed agreement relating to the NICTRIC voyage charter, which he requested Schnitzer to execute. Fletcher's draft of the first paragraph read (Ex. 115):

- "1. Sub-Charterer agrees to remain responsible for the entire demurrage and unpaid freight and any other sums due or to become due under said sub-charter *without Time-Charterer first exercising a lien on the cargo as required by Section 8 of said charter.*" [emphasis supplied]

Fletcher plainly realized, contrary to the Court's findings, that exercise of the lien on the cargo by Amtro was required by Clause 8 of the charter party, as a condition to the existence of Schnitzer's liability for demurrage and unpaid freight.

Fletcher by his own testimony threatened exercise of the lien orally on November 13, 1961 (Tr. 105). Mr. Fletcher testified to a telephone argument with Mr. Krause, Schnitzer's counsel, on November 17, 1961, in which Fletcher said Amtro had a lien on the cargo for demurrage and unpaid freight and would exercise it unless Schnitzer gave security for the sums (Tr. 107). According to Fletcher, Mr. Krause at this time took the position that the demurrage was not due and the lien not exercisable until completion of discharge (Tr. 107). Fletcher at the same time was arranging with Owners for exercise of the lien on the cargo (Tr. 110). In further communications with Schnitzer's counsel, Fletcher took the position on behalf of Amtro that it would exercise the lien against the cargo under Clause 8 unless Schnitzer acted to post security for the unloading demurrage (Ex. 67, 68, 69, 118, 120; Tr. 224).

Acting pursuant to arrangements made by Amtro's counsel with the owners of the vessel, Dodwell & Co. (Owners' Tokyo agent) on November 27, 1961, wrote to all receivers of the NICTRIC cargo, stating that exercise of the lien on cargo had been ordered unless the consignees paid or gave security for their proportionate share of the accruing demurrage (Ex. 113; Ex. 44E, pp. 16-17; Ex. 44G, p. 159).

In short, Amtro's position throughout its attempts to force Schnitzer to pay the unloading demurrage was that it had a lien on the cargo for the demurrage and unpaid freight and that it would be exercised, unless Schnitzer paid or gave security for these sums and waived the cesser clause requiring Amtro to exercise the lien. Schnitzer never took the position that Amtro had no lien on the cargo. When Mr. Krause on December 7, 1961, notified Fletcher that Schnitzer denied responsibility for the Japanese demurrage, Fletcher told the owners to proceed with exercise of the lien (Tr. 114). On the witness stand, Mr. Fletcher admitted that Amtro had a lien on the cargo (Tr. 124).

Thus, the only change of position in this litigation is that of Amtro, which now claims that there was no lien on the cargo for demurrage and that Clause 8 of the charter party was not in effect. Amtro's present position is an afterthought, occurring when the insufficiency of evidence on inability to exercise the lien became apparent.

Effect of Sale Contracts on Liability for Demurrage

In support of its conclusion that the lien of the cesser clause was not intended to be operative, the Court also found that all of Schnitzer's contracts for sale of cargo, with one exception, provided that liability for demurrage at the unloading port, as between Schnitzer and its buyers, was upon Schnitzer (R. 142, lines 2-4). The Court's implication is that Schnitzer is ultimately liable, in any event, for the unloading demurrage.

The Court's construction of the sale contracts is erroneous. With the exception of one buyer (Mitsui), the contracts did not provide that demurrage was for Schnitzer's account. The Court's suggestion that Schnitzer would be ultimately liable to the buyers for demurrage overlooks not only the terms of the contracts themselves, but also other provisions governing the relations between Schnitzer and its customers, principally the fact that the charter party was incorporated in the bills of lading.

In only three of the eight sale contracts was the subject of demurrage at the unloading port expressly mentioned. Okaya expressly agreed to pay the demurrage (Ex. 112; R. 142). The two Mitsui contracts guaranteed customary quick dispatch ("C.Q.D."), with buyer paying stevedore charges, but provided that demurrage was for "seller's account" (Exs. 18, 19). In seven of the eight sale contracts (Exs. 16, 18, 19, 20, 109, 111, 112), including the two with Mitsui, the buyer expressly agreed to arrange and be responsible for discharge of the cargo from the vessel, or bought "FO" (free out), meaning

that the buyer, not the shipper, is responsible for unloading the vessel. See *St. Ioannis Shipping Corp. v. Ziddell Explorations, Inc.*, 222 F. Supp. 299, 305 (D. Or. 1963), *affm'd*. 336 F.2d 194. The sales under all of the contracts were "C & F" or "CIF," which places responsibility for discharge of the vessel on the buyer. See 2 WILLISTON ON SALES (Rev. ed.) Sec. 280n and 280o. Only in Ex. 110, the Kuwamasa contract, is there any ambiguity in responsibility for discharge. The sale terms of that contract are "CIF (Berth Terms)." Berth terms contemplate the buyer receiving delivery upon the dock, rather than from the vessel, whereas CIF specifies buyer's responsibility for discharge from the vessel. Moreover, four of the sale contracts (Exs. 16, 109, 111, 112) specifically stated "charter party bills of lading acceptable," obviously contemplating incorporation of the charter party terms in the bills of lading.

All bills of lading on the NICTRIC cargo did, in fact, incorporate the terms of the charter party. See Exs. 4-13. This obviously included the lien provisions of the cesser clause and the stipulated periods for loading and discharge in Clauses 18 and 19, after which demurrage would accrue. The trial court completely overlooked these facts in suggesting that Schnitzer, rather than the receivers of the cargo, was ultimately liable for the unloading demurrage.

Where cargo is accepted on discharge under bills of lading incorporating a charter party with a cesser clause or stipulating an agreed time for or rate of discharge, the ultimate liability for demurrage at the discharge port is upon the receivers of the cargo, and not

the vessel or the charterer-shipper. *Yone Suzuki v. Central Argentine Railway*, 27 F.2d 795, 800, 805 (C.C.A. 2, 1928), cert. den. 278 U.S. 652; *The Hans Maersk*, 266 Fed. 806 (C.C.A. 2, 1920); *The Hartismere*, 18 F. SUPP. 767, 1937 A.M.C. 594 (D. Md. 1937); Poor, CHARTER PARTIES AND OCEAN BILLS OF LADING (4th ed. 1954) Sec. 27; Tiberg, THE CLAIM FOR DEMURRAGE (1962) Ch. II, p. 15 et seq. One who accepts cargo under a bill of lading incorporating such provisions impliedly so agrees. See *Yone Suzuki v. Central Argentine Railway*, supra, 27 F.2d at 800-801.

Thus, all receivers of the cargo in this case took delivery under bills of lading incorporating a charter party with a cesser clause and a specified time for discharge, and thereby impliedly agreed to assume the liability for demurrage at the unloading port which was created by shipment and delivery on these terms. Receipt of cargo under bills of lading incorporating charter party terms rendering receivers liable for demurrage and unpaid freight prevails over any conflicting terms in a sale contract. *Taylor v. Fall River Iron Works*, 124 F. 826 (S.D.N.Y. 1903).

The same would be true under Japanese law, which holds that each consignee was responsible for payment of all demurrage accrued on the cargo covered by the bill of lading that was negotiated to it. See testimony of Prof. Tanikawa, Ex. 44J, pp. 231-233.

The ultimate liability of the cargo buyers for unloading demurrage was recognized by Amtro's counsel, Mr. Fletcher, who wrote to them on December 21, 1962, a year after this case was filed, to demand payment of the demurrage (Ex. 106, 107, 107-A).

Conclusion

The trial court plainly erred in construing the lien provisions of Clause 8 of the charter party to have been modified out of existence. There was no conflict between the allocation of liability for demurrage in Clause 8 and any other clause of the charter party. All parties took the position, until after this case was begun, that Clause 8 and its lien provisions were in effect. By accepting the cargo under bills of lading incorporating the charter party into them, the receivers of the cargo assumed liability for the unloading demurrage, as specified in the cesser clause. Schnitzer's sale contracts with its buyers and the control of discharge by the buyers are consistent with, if not additional grounds for the ultimate liability of the buyers for the unloading demurrage.

II

The Court erred in holding that the condition of Amtro's inability to exercise its lien on the cargo should not be enforced against Amtro, in admitting and relying on hearsay relating to Amtro's alleged inability to exercise the lien, and in holding that the Japanese statutory lien could not be exercised.

(Specifications of Error Nos. 5-18)

As an alternative basis for its decree against Schnitzer for the unpaid freight and demurrage, the Court held that the condition in Clause 8 of the charter party of Amtro's inability to exercise the lien on cargo should not be enforced against Amtro (R. 144). The Court also found that a lien under Japanese law on cargo in the

hands of consignees within a two-week period after delivery could not be exercised because delivery had been to third-party purchasers from the consignees (R. 142-143, 144).

The District Court did not expressly find or conclude that Amtro, in the language of Clause 8 of the charter party, was "unable to obtain payment [of the demurrage and unpaid freight] by exercising the lien on the cargo." Instead, the Court apparently placed the burden of proof on Schnitzer and found against arguments and evidence of Schnitzer showing how the lien could have been exercised (R. 142-144). It also held that "Amtro was not in a position to effectively assert its lien on account of the representations of Schnitzer that the demurrage and unpaid freight would be paid" (R. 144). The Court therefore concluded:

"Even if Clause 8 remained in full force and effect, not modified by the typewritten language, the provision with reference to the exercise of the lien being the sole remedy, it should not be enforced on the record before me." (R. 144)

Thus, the Court seems to be invoking some sort of estoppel or equitable bar to Schnitzer insisting on proof of the condition to its liability provided in Clause 8, rather than finding that Amtro's inability to exercise the lien was proved.

No Substantial Evidence that Amtro Unable to Exercise Lien

To the extent that the Court's opinion may be read as a finding and conclusion that Amtro was unable to exercise its lien upon the cargo for unpaid freight and

demurrage, there is no substantial evidence in the record to support it. Amtro clearly did not exercise the lien. Clause 8 requires Amtro to establish that it was "unable" to do so, before Schnitzer is liable. This calls, at the very least, for a showing of unsuccessful attempts to exercise the lien, or proof of conditions demonstrating that attempts to exercise the lien in any fashion would have been futile gestures..

Under Clause 8 of the charter party, the burden is upon Amtro to show that the lien on cargo could not be exercised, as a condition of Schnitzer's liability for the unpaid freight and demurrage. It was expressly so held by the arbitrators under an identical cesser clause in *The Luossa*, 1936 A.M.C. 213 (1935). See also *The Arizpa*, 63 F.2d 42, 43 (C.C.A. 4, 1933); Tiberg, *THE CLAIM FOR DEMURRAGE* (1962), p. 55.

All evidence relating to failure or alleged inability to exercise the lien on cargo was in the form of depositions or other documentary materials. In this situation, an appellate court lacks no advantage of the trial court in evaluating the evidence, and properly accords less presumptive validity to findings of the trial court based on such evidence. See, for example, the decisions of this Court in *The Ernest H. Meyer*, 84 F.2d 496, 500-501 (1936), cert. den 299 U.S. 600; *Johnson v. Griffiths*, 150 F.2d 224 (1945); *Murphey v. U.S.*, 179 F.2d 743, 744-745 (1950); *American Eagle Fire Insurance Co. v. Eagle Star Insurance Co.*, 216 F.2d 176, 179 (1954). Other Courts of Appeals follow this practice when the evidence on an issue is mostly in written form. *Iravani Mottaghi v. Barkey Importing Co.*, 244 F.2d 238, 248

(C.A. 2, 1957), cert. den. 354 U.S. 939; *Dollar v. Land*, 184 F.2d 245, 248-249 (C.A. D.C., 1950), cert. den. 340 U.S. 884; *Spanos v. The Lily*, 261 F.2d 214-215 (C.A. 4, 1958). The three decisions last cited make it clear that the lesser presumption given findings based on written evidence is but a common-sense application of the "clearly erroneous" rule of *McAllister v. U.S.*, 348 U.S. 19 (1954), which requires the appellate court to examine the entire evidence on a challenged finding.

The evidence demonstrates that exercise of the lien against cargo was considered by Amtro and Owners only between November 24, 1961, and December 10, 1961, when a decision was made to bring suit against Schnitzer in Oregon for the demurrage and unpaid freight. After December 10, efforts of the Japanese agents and attorneys were directed toward collecting "proof" that the exercise of the lien was impossible because of port congestion. The vessel was discharging cargo from December 3, 1961, until December 31, 1961 (R. 105), and this suit was filed on December 14, 1961 (R. 1).

In this entire period of November 24, 1961, to December 31, 1961, the only external efforts to exercise the lien were letters of Dodwell & Co. to Japanese consignees on November 27, mildly and unsuccessfully requesting payment of the demurrage (Ex. 113; Dep. Ex. F-1; Ex. 44 E, p. 15; Ex. 44 G., p. 159), with no follow-up whatsoever, and Dodwell's unsuccessful request to eight stevedore firms on December 12, 1961, for lighters in which to discharge the cargo for lien purposes (Dep. Ex. B-3 - B-8; Ex. 44E, pp. 22, 52-52-A).

Saishoji did nothing other than contact eight stevedores on December 12, 1961. He testified on cross-examination:

“Q. . . . The only things you did, was to contact the stevedore companies?”

A. Yes.

Q. You personally did nothing else.

A. No, that was the job for other departments.

Q. Your only contact with the whole demurrage case, and the exercise of the lien, was to contact stevedores?

A. Yes.” (Ex. 44 E, pp. 133-134)

As argued below, the December 12 contact with stevedores was part of the process of gathering evidence of inability to exercise the lien, after a decision had been made to sue Schnitzer in the United States.

Main did nothing other than his letter to the consignees (Ex. 113) on November 27, 1961. He testified on cross-examination:

“Q. . . . Other than this letter, you didn’t do anything to lien the cargo on the ‘NICTRIC’ except for conferring with your assistants, or directing them or whatever, is that right?

A. Yes.”

(Ex. 44 G., p. 166)

Mr. Stewart of Amtro did nothing toward exercise of the lien except to discuss it with Morgan (Tr. 79-81). Morgan claimed to have inquired on December 8, 1961, of a stevedore representative about lighters, but admitted on cross-examination that he could not remember the

name of the company (Ex. 44F, pp. 77, 144). He also admitted that he did nothing after December 8, 1961, to exercise the lien (Ex. 44F, p. 110).

A chronological summary of the correspondence and cables between Amtro, Owners and their Japanese representatives will demonstrate the *pro forma* nature of any desire or attempt to exercise the lien, particularly after the decision was made to bring suit against Schnitzer. The first evidence of any arrangements to exercise the lien is the testimony of Amtro's attorney, Mr. Fletcher, that between November 20 and November 25, 1961, he told Owners' New York attorneys to arrange for it (Tr. 110), to which they agreed (Tr. 111). On November 24, 1961, Dodwell & Co., Owners' agents in Tokyo, received advice of this from Owners, and was instructed to make demand, in conjunction with Owners' Tokyo counsel (the McIvor firm), on the consignees for payment of accrued demurrage and unpaid freight (Dep. Ex. B-17; Ex. 44E, pp. 19, 132). As noted above, letters were sent to the consignees on November 27 (Ex. 113, Dep. Ex. F-1; Ex. 44E, p. 15; Ex. 44G, p. 159). This produced no results except the denial of liability by two of the consignees on November 29 (Dep. Exs. F-2, F-3; Ex. 44E, pp. 17-18; Ex. 44G, p. 159).

On November 29, Owners cabled Dodwell instructing immediate exercise of the lien (Dep. Ex. B-24). Dodwell meanwhile had contacted the McIvor firm about this, and so reported to the Owners (Dep. Ex. B-16; Ex. 44E, pp. 20, 123; Dep. Ex. B-20, B-25; Ex. 44G, p. 177-1). Captain Cassimatis, Master of the NICTRIC (then lying in Tokyo harbor), in late No-

vember cabled Owners that he agreed with exercise of the lien, and stated "do not anticipate any difficulties regarding demurrage though settlement takes up to 3 months" (Dep. Ex. B-21). Discharge of the vessel commenced on December 3, 1961 (R. 105).

On December 7, 1961, Mr. Fletcher, Amtro's counsel, was advised by Schnitzer that it would not be responsible for the demurrage, which Fletcher immediately reported to Owners' New York counsel (Tr. 113-114). It was thus clear at this time, if it had not been earlier, that exercise of the lien was going to be necessary, since both Schnitzer and the consignees disclaimed responsibility.

On December 9, 1961, however, Dodwell sent a cable to Owners containing the following report:

" . . . VIEW UNAVAILABILITY LIGHTERS STORAGE SPACE ONLY WAY EXERCISE LIEN IS BY CEASING DISCHARGE AND HOLDING IN SHIP WHICH ACTION OWING CURRENT CONGESTION EMERGENCY MEASURES WILL RESULT IN PORT AUTHORITIES ORDERING NICTRIC OUT OF BERTH NECESSITATING AWAITING TURN LATER FOR REALLOCATION BERTH INCURRING FURTHER DELAY THEREFORE IMMEDIATE LIEN ACTION UNADVISABLE BEST WAIT UNTIL ABOUT 1500 TONS CARGO REMAINING IF LIEN STILL NECESSARY AT THAT TIME. ENDEAVORING NEGOTIATE WITH CHARTERERS REPRESENTATIVES MEANWHILE SCHNITZER LEFT JAPAN RETURNED USA. CONSULTED McIVORS WHO ADVISE VIEW CHARTER COMPLICATIONS LITIGATION JAPAN

SHOULD BE AVOIDED IF POSSIBLE CONSEQUENTLY RECOMMEND YOU CONTINUE EFFORTS GUARANTEE FROM VOYAGE CHARTERERS *MEANWHILE WE WILL EMPHASIZE TO RECEIVERS INTENDED LIEN* AND POSSIBLY THEY WILL PRESSURIZE SCHNITZER GIVE SECURITY." (Dep. Ex. F 4, emphasis supplied; Ex. 44E 20-22; Ex. 44G 171-172)

There is no evidence that Dodwell after sending this cable told receivers of the intended exercise of the lien or, in fact, had any further contact with the receivers. Owners replied to this report by cable to Dodwell on December 10, 1961, to the effect that its New York attorneys had decided to bring suit in Oregon and garnish Schnitzer for demurrage monies, and instructed Dodwell to have McIvor submit proof of impossibility of lien exercise to the Owners' New York attorneys (Dep. Ex. B-23).

Dodwell's cable of December 9 (Dep. Ex. F-4, quoted above) is not, of course, proof in this case of the facts it reported to Owners. As of this cable, the only evidence of any activity whatever to exercise the lien was the letter of Dodwell to the consignees on November 27, 1961 (Ex. 113; Dep. Ex. F-1). There is no testimony that anyone ever contacted the harbor authorities about holding the cargo on board or using lighters for possession of the cargo during exercise of the lien. It was Dodwell's recommendation that exercise be delayed until 1500 tons remained on board.

The only thing done after this exchange of cables on December 9 and December 10 (Exs. F-4, B-23) was Mr. Saishoji's contact for Dodwell & Co. on December

12 of eight stevedore companies in the Tokyo area (Ex. 44E, p. 22, 52-52A; Dep. Ex. B-3 - B-8), six of whom dutifully signed the form at the foot of Dodwell's letter acknowledging that they could not furnish lighters for exercise of the lien (Dep. Ex. B-3 - B-8).

Mr. Fletcher testified (Tr. 115) that he was told on December 11 by Owners' New York attorneys that McIvor reported that exercise of the lien against the cargo was impossible. No witness or document from the McIvor firm was introduced to support this double hearsay. In fact, the McIvor firm seems not to have been given all the facts, and had advised only that it might be safer to sue Schnitzer than to exercise the lien. In a letter to Dodwell dated December 13, 1961, the McIvor firm stated:

" . . . We agree that Owners are still advised to obtain satisfaction from charterers since *unless the bills of lading are properly cloused*, they would have no right to lien the cargo for the demurrage. In addition, the existence of the voyage charter would complicate any legal action in Japan thereby making it difficult to bear pressure on the consignees.

"For your records we set forth below a copy of cable received yesterday from Mainbrace:

" 'NICTRIC PLEASE OBTAIN DETAIL PROOF OF IMPOSSIBLITY LIENING CARGO ACCORDANCE WILSON REPORT AND FORWARD TO US ALSO PLEASE ADVISE APPROXIMATE DATE COMPLETION DISCHARGE'

and we note that you are proceeding to obtain and we note that you are proceeding to obtain the necessary proof." (Dep. Ex. B-18, emphasis supplied; see also Dep. Ex. F-4, quoted *supra*)

In fact, the bills of lading were "properly claused," incorporating the charter party cesser clause. Mr. Main of Dodwell & Co. admitted (Ex. 44G, p. 177-2) that the McIvor firm never advised Dodwell & Co. that exercise of the lien was impossible, legally or otherwise.

The libel in this case was filed on the following day, December 14, 1961 (R. 1). There is no evidence of any further efforts whatever to exercise the lien, and in fact there were no efforts after Mr. Saishoji's contact with eight stevedoring firms on December 12, requesting the use of lighters.

When discharge was nearing completion, Dodwell & Co. cabled Owners on December 26 as follows:

"NICTRIC GUIDANCE RECEIVERS ENDEAVOURING COMPLETE BY THIRTY FIRST AND ALTHOUGH DOUBTFUL VIEW ONLY ABOUT 1200 TONS NOW REMAINING FEEL IF LIEN NECESSARY MUST ACT IMMEDIATELY. McIVORS ADVISED. PLEASE INSTRUCT." (Dep. Ex. B-19; Ex. 44G, p. 177-2)

To this, Owners replied on December 28 by cable to Dodwell:

"NICTRIC YOURTEL 26TH UNDERSTAND FROM McIVOR THAT LIEN IMPOSSIBLE THEREFORE CLUB PROCEEDING AGAINST VOYAGE CHARTERERS PORTLAND NEVERTHELESS ENDEAVOUR EXERCISE LIEN VIEW KEEPING VOYAGE CHARTERERS RESPONSIBLE UNDER CLAUSE 8 VOYAGE CHARTER. . . ." (Dep. Ex B-2, emphasis supplied; Ex. 44E, p. 42, 7x. 44G, p. 177-2)

These two cables confirm that efforts concerning ex-

ercise of the lien after the libel was filed on December 14, 1961, were simply motions to "endeavour exercise lien view keeping voyage charterers responsible under Clause 8 voyage charter," in the words of the December 28 cable.

The total cargo carried by the NICTRIC was 8,991.14 long tons (Exs. 4-13). On the basis of prices paid by the Japanese buyers for the cargo delivered to Tokyo, its value in Tokyo harbor was about \$500,000 (see Tr. 196; Exs. 16, 18-20, 109-112), or more than \$50 per long ton. Assuming a steady rate of discharge from beginning to end (December 3-December 31, 1961), half the cargo (value at least \$225,000) remained on board on December 18, ten days after Schnitzer disclaimed liability. The 1500-ton point (value at least \$75,000) was not reached until about December 24. As late as December 26, when Dodwell cabled that 1200 tons remained on board, the vessel could have ceased discharging and kept cargo in its possession worth at least \$60,000.

The question thus boils down to this: is the evidence offered of alleged inability of eight stevedore firms to furnish lighters to exercise the lien sufficient to permit a finding that Amtro was unable to exercise its lien on the cargo under the circumstances shown by the record, thus fulfilling its obligations under Clause 8 of the charter party? There are 20 large stevedoring firms and some 50 smaller ones in the Tokyo harbor area (Ex. 44H, p. 187-1). No attempt was made to secure lighters from any other firms or from any firm at any time other than December 12 Ex. 44E, p. 22, 126; Ex. 44G, p. 163). No method for exercising the lien was considered or at-

tempted by Amtro or Owners other than discharge into lighters (Ex. 44E, p. 136). No attempt was made to exercise the lien by stopping discharge and holding the cargo on board the vessel (Ex. 44E, p. 59; Ex. 44G, pp. 160, 168), or to inquire about partial discharge for lien purposes at a special seven-day berth (Ex. 44G, p. 168-169; Ex. 44H, p. 187-2, et seq.), or to explore any other means of exercising the lien. The Dodwell employees admitted that the contact of the eight stevedore firms on December 12 was the only thing that anyone did toward exercise of the lien (Ex. 44E, pp. 126-127; Ex. 44G, p. 163).

Other than citing the contact of eight stevedore firms on December 12, 1961, by Dodwell & Co., the Court's opinion, like Amtro's argument, is devoted to exposition of why any other efforts to exercise the lien would have proved unsuccessful. No attempt was made to cease discharging or to hold the cargo on board the vessel (Ex. 44 E, p. 59). The Court found that the vessel, had it done so, "risked . . . the probability of being moved by the harbor authorities and sent to anchor outside to wait another turn at discharge," behind some 50 to 100 other waiting ships. See also R. 143.

There is no substantial evidence to support this finding (see Specification of Error No. 6). No Japanese harbor authority was called as a witness, and no law, regulation or custom of the port was proved. Saishoji and Main speculated that this might occur (Ex. 44E, pp. 24-25; Ex. 44G, 160, 177-3, 177-4), but this was clearly hearsay and opinion based on matters outside the record (see Specifications of Error Nos. 12(b) and (c),

16(a), (d) and (e)). They made no inquiry to the harbor authorities about stopping discharge on the NICTRIC (Ex. 44E, pp. 62, 64, Ex. 44G, p. 162).

Saishoji admitted that he had no personal knowledge concerning exercise of the lien on the NICTRIC, except his contact with eight stevedore firms on December 12: "I was told by Mr. Main that the lien was impossible" (Ex. 44 E., p. 126, and see pp. 129, 133-134).

Main's sole actions relative to the NICTRIC lien exercise were to direct his assistants at Dodwell & Co., and his testimony obviously must have come from what they told him:

"Q. [by Mr. Lewis] . . . What did you personally have to do with the attempt to lien the 'NIC-TRIC' cargo?

A. My personal actions would be to direct the Japanese staff concerned to take the action which I considered necessary to meet the occasion.

Q. Certainly, but your action then would be with your staff, is that right?

A. Yes.

Q. But as far as attempts to lien the 'NICTRIC' cargo, did you personally do anything other than to confer with your assistants?

A. No, just conferred with my assistants." (Ex. 44 G., p. 162).

See also Ex. 44 G., pp. 163, 172.

That exercise of the lien may have delayed the vessel further is no excuse for Amtro's failure to exercise it. The result would only have been additional demurrage charges by the vessel to collect out of the exercise of the

lien on the cargo. As shown above, there was cargo on board the NICTRIC worth 15 times as much as the demurrage awarded here for a period of almost three months. If exercise of the lien did not produce sufficient sums to pay all demurrage and expenses of exercise, the lien was to that extent not commensurate with the liability it was intended to secure, and Amtro could have recovered against Schnitzer any deficiency remaining after exercise of the lien. *Crossman v. Burrill*, 179 U.S. 100 (1900). Amtro's counsel, Mr. Fletcher, made the same point in his original demand of November 10, 1961, on Schnitzer (Ex. 101):

“ . . . AS YOU KNOW EXERCISE LIEN IN JAPAN OR TAKING CARGO ELSEWHERE WILL CAUSE GREAT EXPENSE AND ADDITIONAL DELAY OF VESSEL WHICH WILL GO TO REDUCE PROCEEDS OF LIEN EXERCISE AND ADD TO YOUR LIABILITY FOR DEFICIENCY UNDER CHARTER . . . ”

The Court also rejected (R. 143) Schnitzer's uncontradicted evidence that discharge for purposes of exercising the lien could have occurred without lighters by moving the vessel to Harumi wharf, a special scrap-discharge berth where a vessel could remain only seven days. It found that this facility could not have been used because the entire cargo could not have been discharged within seven days (R. 143). This finding and the evidence cited by the Court to support it are the subjects of Specification of Error No. 7.

Mr. Koizumi of Pacific Marine Corporation, the Japanese agent of Amtro and Schnitzer for this voyage, testified that these facilities were available and could have

been used for this purpose (Ex 4H, pp. 187-1, et seq.). He testified that 4,500 tons could have been discharged there in seven days (Ex. 44 H., p. 187-17). At \$50 per ton, that amount of cargo would have been worth \$225,000, far more than the amounts in issue. Bonded space for storage until resale was also available there (Ex. 44 H., p. 187-3, 187-4). Also, lighters could discharge at that wharf (Ex. 44 H., p. 187-5). Although Dodwell advised Owners on December 9 to wait until 1500 tons remained before exercising the lien (Dep. Ex. F-4), neither Dodwell nor anyone else made any effort to arrange or schedule discharge at Harumi wharf when the cargo was discharged to that point. While all the cargo could not have been discharged in seven days at Harumi, there is uncontradicted evidence that a sufficient part of it to exercise the lien could have been discharged there within that time, and that there was absolutely no inquiry or attempt to arrange this by Amtro or Owners or their agents (Ex. 44 G., pp. 168-169). Dodwell considered exercise of the lien only by discharge into lighters (Ex. 44 E., p. 136).

The Court's holding that exercise of the lien could not have occurred through discharge at Harumi wharf was based upon the following finding (R. 143):

"Schnitzer's agent tried to put the vessel in at this particular wharf, but could not do so on account of the nature of the vessel's scrap."

This finding is unsupported by substantial evidence (Specification of Error No. 7), since the only possible basis for it is hearsay and self-serving material found in Dep. Ex. B-11, a letter dated January 9, 1962, from

F. A. L. Morgan, Amtro's Far-Eastern representative, to Amtro. The objection to its admissibility was asserted in the trial court (R. 127-128) and overruled (R. 186). It is the subject of Specification of Error No. 14 on this appeal.

Ex. B-11 was produced in Morgan's deposition (Ex. 44F, pp. 89 et seq.) by Owners' counsel in cross-examination concerning efforts to locate a cargo for the NICTRIC's return voyage, not in relation to the lien issue. In the course of a long report to Amtro, Morgan wrote:

"During my visit to Tokyo in the period 21st October to 8th November, Schnitzer Steel Products' Tokyo representative, Mr. Morgulis, had been endeavoring to arrange for the Nictric to discharge out of turn at a special quick discharge berth, but subsequently gave up the idea because of the Nictric's varied types of scrap cargo which would not admit of completion within seven days." (Ex. B-11, p. 1)

Morgan failed to give any such testimony in his deposition, and the letter was written over a month after this case was filed. The letter was from one Amtro official to another. Morgan does not state the source of his information, nor whether the quoted statement is his personal knowledge. The quoted portion of Ex. B-11, relied upon by the Court, is plainly hearsay and inadmissible against Schnitzer. The Court's overruling of Schnitzer's objection to it (R. 186) and reliance on it is plainly prejudicial error.

The Court also found that no bonded space in

all of Tokyo harbor was available for retaining possession of the cargo ashore while the lien was exercised (R. 143). The lack of evidence to support this finding is the subject of Specification of Error No. 9. To the contrary was the testimony of Koizumi that bonded storage space was available at Harumi wharf (Ex. 44H, p. 187-3, 187-4). Since Main lacked personal knowledge, as pointed out earlier, his testimony on unavailability of storage space was hearsay opinion, not based on any inquiry on his part. See Specifications of Error No. 16(c) and (d). The hearsay character of similar testimony by Morgan is plain from Morgan's own testimony, in which he admits that his testimony was an opinion told to him by a stevedoring firm (Ex. 44F, p. 77); Specification of Error No. 13).

The only evidence cited by the Court (R. 143) for this finding is Dep. Ex. F-23, a newsletter published by Pacific Marine Corp of Tokyo dated September 15, 1961. The newsletter was prepared for circulation to the firm's customers for general information, having been compiled from numerous reports, opinions and miscellaneous other sources (Ex. 44H, p. 187-23, et seq.). The report's statements at p. 6 about lack of storage space are quoted by the Court (R. 143). Koizumi was unable to say that this report was sent to Schnitzer (Ex. 44H, p. 187-23).

This report (Ex. F-23) was objected to by Schnitzer as hearsay (R. 127-128), but the objection was overruled by the Court (R. 186). This ruling constitutes the subject of Specification of Error No. 15 on

this appeal. Koizumi admitted that the matters in the report were not necessarily from personal knowledge of those publishing it (Ex. 44H, p. 187-28). Koizumi was not asked as to his personal knowledge on this aspect of the report, except that he testified that storage space was available at Harumi wharf (Ex. 44H, p. 187-3).

Dep. Ex. F-23 was not admissible under the hearsay exception for records kept in the ordinary course of business. It is not an entry in the books of the business. This type of report falls within few, if any of the elements required for admissibility under this hearsay exception, as set forth in McCormick, EVIDENCE (Hornbook Series 1954), pp. 596 et seq. It has no more standing as evidence than a newspaper article. It was, in fact, denominated a "Newsletter" (Dep. Ex. F-23, p. 1). Finally, a report on conditions as of September 15, 1961 has no relevance to conditions bearing on exercise of the lien three months later in December, 1961.

The Court further found (R. 144; Specification of Error No. 8) that Japanese port authorities would not have permitted cargo to be kept in Amtro's possession aboard lighters while the lien was exercised. Here again, the finding could only have been based upon the conjectural and hearsay testimony of Saishoji (Ex. 44E, p. 23, 34A-35) and of Main (Ex. 44G, pp. 173, 177-3, 177-4). See Specifications of Error Nos. 12(a) and (d), 16(c) and (d). No inquiry to harbor officials was made (Ex. 44E, pp. 62, 64), and Saishoji and Main had no personal knowledge, as the challenged testimony indicates.

Saishoji's main reason for his testimony was that the lighter owners would not, in his opinion, accept demurrage rates while the lien was exercised and they preferred to serve the greater needs of their regular customers (Ex. 44E, p. 23, 34A-35). There was no requirement that Amtro pay merely demurrage rates for use of the lighters in exercising the lien. The expenses of exercising the lien, including full charges for use of lighters and storage expense, are recoverable from the proceeds of the lien, or against the charterer to the extent that the proceeds are insufficient to pay expenses and the principal sums due. *The Asiatic Prince* 103 Fed. 676, 677 (E.D. N.Y. 1900), *aff'd*. 108 Fed. 287, *cert. den.* 183 U.S. 697; Tiberg. *THE CLAIM FOR DEMURRAGE* (1962) p 76.

Saishoji testified that lighters could discharge at Harumi wharf on two-weeks' notice (Ex. 44H, p. 187-5). Dodwell in its December 9 cable to Owners (Dep. Ex. F-4) recommended that the lien be exercised on the last 1,500 tons of cargo, but took no steps whatever to apply or inquire about reserving space at Harumi wharf or elsewhere when that point was reached (Ex. 44G, pp. 168-169). Since 1,200 tons remained on December 26 (Dep. Ex. B-19), at least 1,500 tons would have been on board within two week after December 9, and much more on board two weeks after Dodwell was first instructed on November 24, 1961, to arrange for exercise of the lien (Dep. Ex. B-24, Ex 44E, pp. 19, 32).

In short, the Court's findings on matters of Amtro's inability to exercise the lien are unsupported by substantial evidence, and shot through with reliance

on hearsay to which Schnitzer's objections were overruled.

We have found no cases precisely in point as to what constitutes inability to exercise a lien on cargo within the meaning of the cesser clause. Recovery of unpaid freight and demurrage against the charterer was denied in two cases involving the GENCON form cesser clause, for lack of proof by the vessel owner of any effort whatever to exercise the lien. *The Luossa*, 1936 A.M.C. 213 (Arb. 1935); "*Z*" *Steamship Co. v. Amtorg New York*, 61 Lloyd's List L.R. 97 (K. B. Div. 1938). These decisions establish, of course, that the burden is upon the vessel owner to show its inability to exercise the lien against cargo, before it can recover unpaid freight and the unloading demurrage from the charterer.

Similar results are reached under other cesser clauses in which the charterer's liability ceases upon loading of the cargo, except to the extent that the ship's lien is not commensurate with the liability it is intended to cover. Failure of the ship to prove inability to exercise the lien prevents recovery of unloading demurrage from the charterer under this form of cesser clause. *The Arizpa*, 62 F.2d 42 (C.C.A. 4, 1933), cert. den. 290 U.S. 648; *The Eastern Bell*, 1923 A.M.C. 271 (W.D. Wash. 1923).

At the very least, the condition of inability to exercise the lien on cargo stated in Clause 8 of the charter party requires Amtro to prove good-faith efforts to exercise the lien and inability to exercise it because of conditions beyond its control. The evidence here falls

far short of that standard. Amtro and Owners did nothing beyond contacting eight of the numerous stevedoring firms in Tokyo harbor on December 12, when the decision had already been made to sue Schnitzer. Despite the advice of Dodwell & Co., their agents, on December 9, 1961, to delay exercise of the lien until only 1,500 tons of cargo remained on board, nothing whatever was done thereafter to make the necessary arrangements for exercise of the lien when discharging reached that point about December 24.

The record does not even show that a positive threat to exercise the lien was ever communicated by Amtro or Owners to the consignees, after the latter failed to pay or give security for the unpaid freight and demurrage. Dodwell & Co. handled over 100 vessels on demurrage in the congestion period during which the NIC-TRIC was in Tokyo harbor, and in most cases obtained guarantees of the receivers to pay the demurrage (Ex. 44G, pp. 154-156). To do so undoubtedly required Dodwell to make it known to the consignees that the lien would be exercised unless they met their responsibility. In view of the mild tone of the only letter of Dodwell to the consignees in this case (Ex. 113), it is not surprising that the consignees felt no pressure to assume their liability for the demurrage and unpaid freight. There was no real intent or effort ever manifested by Amtro or Owners to exercise the lien against the cargo.

The uncontradicted evidence indicates that there were in fact no efforts whatever made to exercise the lien after the libel was filed in this case on December

14, 1961, despite the fact that discharge was not completed until December 31, 1961. The allegations in the original and amended libels and the cross-libel that diligent efforts were made to exercise the lien under Clause 8 of the voyage charter party were never substantiated by the evidence.

Failure to Exercise Japanese Statutory Lien

One way to avoid any problem of port congestion was to exercise the lien on cargo in the hands of the Japanese consignees within two weeks after discharge and delivery to them. The Court found that such a lien existed under Japanese law (R. 144), in accordance with testimony given by Japanese legal experts. Ex. 44J, pp. 231, et seq., Dep. Ex. L-4; Ex. 44I, pp. 193, 224. American law recognizes a similar lien. See *Bags of Linseed*, 1 Black 108, 17 L. Ed. 35 (1861).

The Court found, however, that the Japanese statutory lien could not have been exercised because delivery had been to third-party purchasers from the consignees, and not to the consignees (R. 142-143, 144). There is no substantial evidence to support this finding (Specification of Error No. 10). Saishoji's testimony (Ex. 44E, pp. 65-66; Specification of Error No. 12(e)) clearly was hearsay repetition of statements allegedly made to him by the consignees when he inquired of them. Schnitzer's objections to it as such in the trial court (R. 123-125) apparently were not sustained (R. 185).

The cargo discharge survey reports (Exs. 22-27, 29) were offered by Owners in the District Court as show-

ing delivery of the cargo to parties other than the consignees (Tr. 10-12). These reports were certificates of weight and condition of the cargo required by the sale contracts (see Exs. 16, 18-20, 109-112), since payment was to be made on the basis of quantities shown by these reports. These matters were not in issue. The discharge reports certainly were inadmissible to prove passing of title from the consignees or that persons other than the consignees took possession of the cargo upon delivery from the vessel. Schnitzer objected to their admissibility on these grounds, but was overruled by the Court (Tr. 10-12). Error is asserted here (Specification of Error No. 18).

These reports on their face show that their purpose is to measure the character and quantity of cargo discharged, not to reflect ownership or possession of the cargo upon discharge. In designating the consignees and "consumers," the reports could only be reflecting information given by some third party. They do not refer to title documents or state that title or possession had passed to third parties on delivery or any time thereafter. For all these reports show, sale and delivery to consumers by consignees may have been to occur in the future.

No contracts or other evidence of sale or delivery to third parties were offered in evidence. The ship's master or agent receives the bills of lading when cargo is released for discharge, but neither Amtro nor Owners produced any evidence as to whether the consignees or the alleged third parties endorsed or presented the bills of lading in order to receive the cargo.

Thus, there is no evidence supporting a finding that delivery from the vessel was to third parties and not to the consignees, so as to prevent exercise of the Japanese statutory lien. If such delivery was made, Amtro and Owners allowed it to occur, since they alone had the power to refuse delivery to third parties unless the demurrage was paid.

Representations of Schnitzer Did Not Prevent Exercise of Lien

The principal ground of the Court's refusal to enforce the condition specified in Clause 8 to Schnitzer's liability appears to have been the Court's conclusion that "Amtro was not in a position to effectively assert its lien on account of the representations of Schnitzer that the demurrage and unpaid freight would be paid" (R. 144). The Court had found that Schnitzer agreed to pay the sums when first contacted by Amtro on November 13, 1961, but subsequently declined responsibility on December 7, 1961 (R. 140-141). This finding was based (R. 141) on the testimony of Mr. Fletcher (Tr. 104-105, 113).

Accepting Fletcher's testimony, there is no evidence whatever that any such representations of payment deterred or prevented Amtro or Owners from exercising the lien (Specification of Error No. 11). Certainly Fletcher did not so testify. The evidence conclusively disproves the Court's conclusion that Amtro was not in a position to assert its lien on account of Schnitzer's alleged representations.

First, Amtro did nothing in the month following the commencement of demurrage to arrange for exercise of its lien. Amtro obviously knew that the vessel arrived in Japan on August 11 and was then ready to discharge (R. 104). It knew that laytime expired and demurrage began to accrue on October 9, 1961 (R. 105; Tr. 188), and that there would be a substantial delay before the vessel received a discharge berth. Yet Amtro did nothing whatever to arrange for exercise of the lien up to November 10, when it retained Mr. Fletcher to assert demands on Schnitzer (Tr. 53, 103).

Secondly, any representations of payment made by Schnitzer in the period November 13, 1961-December 7, 1961, as found by the Court, clearly did not deter Amtro from starting arrangements to exercise the lien. If such representations were made, Amtro did not rely on them, since Mr. Fletcher between November 20 and November 25 had agreed with Owners' New York attorneys that steps should be immediately undertaken to exercise the lien on cargo (Tr 110-111). Owners cabled Dodwell & Co., their agents, on November 24 to arrange for exercise of the lien (Dep. Ex. B-17; Ex. 44E, pp. 19-32), and Dodwell began the process on November 27 by advising th consignees of its instructions from Owners (Ex. 113; Dep. Ex. F-1, Ex. 44E, p. 15; Ex. 44G, p. 159). Dodwell consulted the McIvor firm about it on November 30 (Dep. Ex. B-20).

Finally, Amtro knew and communicated to Owners on December 7, 1961, that Schnitzer would not pay the demurrage, and Fletcher at that time gave instructions

to proceed with exercise of the lien (Tr. 113-114). This occurred four days after the ship began discharge on December 3, 1961 (R. 105). More than sufficient cargo remained on board for many days after December 7 for Amtro to have collected all sums due it by exercise of its lien. See evidence cited *supra*, p. 60. Dodwell & Co. itself on December 9 had recommended to Owners that exercise be delayed until 1,500 tons remained on board (Dep. Ex. F-4).

In short, anything Schnitzer may have said up to December 7, 1961, obviously did not prevent Amtro and Owners from exercising the lien at any time, had they desired to do so.

Conclusion

Amtro and Owners failed to meet their burden of showing inability to exercise the lien. Almost from the beginning, their efforts were directed toward collecting the demurrage and unpaid freight from Schnitzer, since they believed this would be less troublesome than exercising the lien as Amtro in Clause 8 of the charter party had agreed to do. The evidence shows that Amtro and Owners had no intent and made no good-faith effort to exercise the lien. They confined themselves to collecting "evidence" of their alleged inability to exercise the lien, for use in this case.

The lower court's decision has deprived Schnitzer of the benefits of the cesser clause and its incorporation in the bills of lading. Instead of forcing the consignees to pay the demurrage by exercise of the lien, Amtro

and Owners allowed the primarily liable parties to escape their responsibilities, and now try to put upon Schnitzer the risks and expenses of recovery at this late date against the Japanese buyers, without the pressure of any lien or possessory rights. There is no basis in law or in the facts shown in this record for allowing this injustice to stand by refusing to enforce the provisions of Clause 8 against Amtro.

III

The Court erred in holding that demurrage ran during weekends and holidays as defined in Clause 19 of the charter party.

(Specification of Error No. 19)

Rejecting Schnitzer's contention to the contrary (R. 114), the Court held that Clause 19 of the charter party did not exclude weekends and holidays not used from the period in which demurrage ran (R. 144-145). This resulted in an award for demurrage running continuously after the laytime expired on October 9, 1961 (R. 105). It is agreed that the demurrage award against Schnitzer of \$57,757.10 would be reduced by \$12,483, if the periods specified in Clause 19 were excluded from the demurrage period of October 9, 1961, through December 31, 1961 (R. 105-106).

Clause 19 of the voyage charter party (Ex. 2) provided:

"Time from noon Saturday until 8:00 a.m. Monday not to count unless used, in which case actual time used to count. Time from midnight preceding holiday until 8:00 a.m. the day after

holiday not to count, unless used, in which case actual time used to count."

This clause follows Clause 18, which expressly dealt with computation of the laytime after which demurrage would accrue.

There are two periods "to count" relating to demurrage. The first is counting of the laydays to determine when free time expires and demurrage commences. The second is counting of the demurrage days. Clause 18 expressly deals with counting of laydays. Clause 19, a separate and independent paragraph of the charter party, applies to all counting, both laytime and demurrage days. Had Clause 19 been intended solely for purposes of calculating laydays, its language would logically have been placed in Clause 18 immediately after the phrase "Sundays and holidays excepted unless used, in which actual time used to count." Note that language in the original printed Clause 7 of the GENCON form (Ex. 75), stricken out of the NICTRIC charter (Ex. 2), provided for demurrage being calculated as "running days," i.e., demurrage running continuously after it began to accrue. Clause 19, to the contrary, excludes weekends and holidays from the demurrage days.

The Court held that any ambiguity in Clause 19 should be construed against Schnitzer as author of the charter party (R. 145). We have previously shown that there is no evidence of Schnitzer's authorship of this charter party or the KEHREA charter party (Ex. 76) on which it was based. See argument *supra*, p. 42; Specification of Error No. 2. Clause 19 of the KEHREA

charter party was identical to that for the NICTRIC, except that weekends and holidays in the KEHREA charter party were not to count even if used. There is no evidence in the record as to which of the parties insisted on or made this change after the KEHREA charter party was given by Schnitzer to the charter broker and sent by the broker to Amtro as a sample for discussion (Ex. 76, Tr. 176). There is no basis for holding Schnitzer any more responsible than Amtro for wording of the NICTRIC charter party.

Under Clause 19 of the charter party, weekends and holidays plainly were not to count in any calculation, whether of laydays or of days on demurrage. Thus, \$12,483 for weekends and holidays after the expiration of the laytime was erroneously included in the demurrage award against Schnitzer.

Respectfully submitted,

GUNTHER F. KRAUSE
CARL R. NEIL
KRAUSE, LINDSAY & NAHSTOLL

Proctors for Schnitzer
Steel Products Co.

CERTIFICATE OF COUNSEL

I certify that, in connection with the preparation of this brief, I have examined Rules 18 and 19 of the United States Court of Appeals for the Ninth Circuit, and that in my opinion, the foregoing brief is in full compliance with those rules.

CARL R. NEIL
Of Proctors for
Schnitzer Steel Products Co.

APPENDIX A

TABLE OF EXHIBITS

Exhibit Number	Identified*	Offered*	Received*
1 and 2	5	5	5
4 through 13, inclusive	5	5	5
16	140	140	140
18	10	10	12
19	11	10	12
20	238	238	238
22	140	140	140
23	10-11	10	12
24A, 24B, and 25	140	140	140
26 and 27	11	10	12
29	140	140	140
32	7	7	7
33	17	17	17
34	26	26	26
35 and 36	17	17	17
41, 42 and 43	25	25	25
44A through 44J, inclusive**	133-135	135	[?] 136-137, 240-241; R. 184-186
45	88	88	88
46	17	17	17
47	18	18	25
48	26	26	26
49 and 50	27	27	27
51	35	35	35
52	89	89	90
53 and 54	141	141	141
56	9	9	9
58	59	59	59-60
59	117	117	117
60, 61 and 62	116	116	116

* All references are to pages of the transcript of the trial.

** See Appendix B for table of deposition exhibits.

Exhibit Number	Identified	Offered	Received
63	117-118	118	118
67	108-109	109	109
68	109	109	110
69	111	111	111
70 and 71	112	112	112
72	113	113	113
73 and 74	90	90	90
75	29	29	30
76	35-36	36	36
77	49	49	50
79	98	98	99
80	238	238	238
101	104	104	104
102	237	237	237
103	193	193	194
104	195	195	195
105	214	214	214
106	213	213	213
107 and 107A	214	214	214
109 through 112, inclusive	12	12-13	13
113	126-127	127	127
114	212	212	213
115	105-106	106	106
116	211	211	212
117	213	213	213
118	212	212	212
120	212	212	212
121	213	213	213
125	133	133	133
127 and 128	215	215	215
133 thru 140, incl.	235-236	235-236	
141	215-216	215	216
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APPENDIX B

TABLE OF DEPOSITION EXHIBITS

All of the deposition exhibits were presumably offered in evidence along with the depositions (Tr. 135), and presumably admitted in evidence (see Tr. 136-137, 240-241, R. 184-186). This table lists apposite each deposition exhibit the name of the witness, the exhibit number assigned at the trial to the deposition, and pages of his deposition in which the deposition exhibit was identified or discussed.

Dep. Ex. No.	Witness	Trial Ex. No.	Pages of Deposition
F-1	Saishoji	44E	16-17
(same as Ex. 113 at trial)	Main	44G	159
F-2	Saishoji	44E	17-18
	Main	44G	159
F-3	Saishoji	44E	17-18
	Main	44G	159
F-4	Saishoji	44E	20-22
	Main	44G	171-172
F-5 through F-18, inclusive	Morgan	44F	74-75
F-19 and F-20	Koizumi	44H	187-20
F-21 and F-22	Koizumi	44H	187-22
F-23	Koizumi	44H	187-23
B-1	Saishoji	44E	41-42
B-2	Saishoji	44E	42
B-3 through B-8, inclusive	Saishoji	44E	52-52A
B-9 through B-13, inclusive	Morgan	44F	90
B-14 and B-14A	Saishoji	44E	122
B-15	Saishoji	44E	123
B-16	Saishoji	44E	20, 123
B-17	Saishoji	44E	19, 132
B-18			
B-19	Main	44G	177-2
B-20			

Dep. Ex. No.	Witness	Trial Ex. No.	Pages of Deposition
B-21			
B-22	Main	44G	158
B-23			
B-24, B-25	Main	44G	177-1
B-26			
B-27	Main	44G	177-1
B-28	Main	44G	177-4
L-1	Tanikawa	44J	231
L-2	Tanikawa	44J	229
L-3	Tanikawa	44J	233
L-4	Tanikawa		
Com. Ex. 1	Tanikawa		
Exhibit Number	Identified*	Offered*	Received*
Exhibit Number	Identified*	Offered*	Received*
		Trial	Pages of
Dep. Ex. No.	Witness	Ex. No.	Deposition

FEB 14 1967

No. 20526

United States
COURT OF APPEALS
for the Ninth Circuit

SCHNITZER STEEL PRODUCTS CO.,
a corporation,

Appellant,

v.

CIA. ESTRELLA BLANCA, LTD., as owner
of the SS NICTRIC, and AMTRO
CORPORATION, S.A.,

Appellees.

AMTRO CORPORATION, S.A.,

Cross-Appellant,

v.

SCHNITZER STEEL PRODUCTS CO.,
a corporation, and
CIA. ESTRELLA BLANCA, LTD.,
as Owner of the SS NICTRIC,

Cross-Appellees.

BRIEF OF APPELLEE
CIA. ESTRELLA BLANCA, LTD.

*Upon Appeal from the United States District Court
for the District of Oregon*

HONORABLE JOHN F. KILKENNY, Judge

LOFTON L. TATUM
WOOD, WOOD, TATUM, MOSSER & BROOKE
1310 Yeon Building
Portland, Oregon 97204

*Proctors for Appellee, Cia. Estrella
Blanca, Ltd.*

FILED

STEVENS-NESS LAW PUB. CO., PORTLAND, ORE.

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BRIEF OF APPELLEE
CIA. ESTRELLA BLANCA, LTD.

*Upon Appeal from the United States District Court
for the District of Oregon*

HONORABLE JOHN F. KILKENNY, Judge

STATEMENT OF THE CASE

Appellee adopts the designation of parties used in the
appeal briefs of time charterer and the voyage charter-

er and in the trial court's opinion. Libelant-Appellee is designated as "Owners," the time charterer and Cross-Appellant as "Amtro" and the voyage charterer and Appellant as "Schnitzer."

Also, Owners adopt the statement of the case as made in Amtro's opening brief. Because Schnitzer's appeal is primarily on factual issues decided adversely to Schnitzer by the trial court, a further discussion of the facts will appear in the argument.

I

ANSWER TO SCHNITZER'S GROUP I ARGUMENT

The District Court Properly Construed the Voyage Charter Party to Place Primary Responsibility for Demurrage and Freight Upon Schnitzer

Schnitzer claims the trial court erred in its interpretation of the voyage charter. To sustain its argument, Schnitzer contends that the Court should ignore the specific language of the voyage charter, its authorship and Schnitzer's own interpretation and conduct and apply only the cesser clause, printed Clause 8 of the voyage charter. The trial court properly held that the charter must be construed in its entirety.

The voyage charter in this case (Ex. 2) is basically a printed form which goes under the code name "Gencon," but there were extensive changes typewritten on and over the printed form itself and a lengthy typewritten rider also attached. The original Gencon charter scheme (of which printed Clause 8 upon which Schnitzer relies is a part) can be understood more

clearly by reading it in the context of the other printed clauses of which Clause 8 was a part. To assist in making the analysis from the basic printed form to the form actually used by the parties here, Exhibit 75, an unmarked Gencon form, was introduced in evidence.

The relevant printed clauses of the basic Gencon form read as follows:

"6. Cargo to be received *by merchants* at their risk and expense alongside the vessel not beyond the reach of her tackle and to be discharged in running working days. Time to commence at 1 P.M. if notice of readiness to discharge is given before noon, and at 6 A.M. next working day if notice given during office hours after noon.

"Time lost in waiting for berth to count as discharging time.

"7. Ten running days on demurrage at the rate of per day or pro rata for any part of a day, payable day by day, *to be allowed merchants* altogether at ports of loading and discharge.

"8. Owners shall have a lien on the cargo for freight, dead freight, demurrage and damages for detention. Charterers shall remain responsible for dead freight and demurrage (including damages for detention) incurred at port of discharge, but only to such extent as the owners have been unable to obtain payments thereof by exercising the lien on the cargo." (Emphasis added)

Thus, in the basic printed form, it was "merchants," i.e., cargo receivers, who, apart from Clause 8, were responsible for demurrage. To this, Clause 8 in the printed form added a degree of liability upon charterers for

freight and demurrage in the event owners were unable to exercise the lien granted in Clause 8. The purpose of this Clause was not to limit an otherwise existing liability since nowhere else in the basic printed form is the charterer made liable for freight or demurrage at all.

This entire pattern was wholly changed by the typewritten deletions and additions to the voyage charter in issue. Old Clause 6 and a part of old Clause 7 making "merchants" liable for demurrage as set forth above were stricken. The subject of old Clause 6 is now covered by the new typewritten Clauses 17 and 18 of the typewritten rider, which contain no reference to any obligation of the "merchants." In fact, Clause 17 places the responsibility for discharging the vessel squarely upon the charterer, not the receivers. Clause 18 contains an unqualified agreement that if the vessel is longer delayed, the charterer would pay the demurrage. These typewritten clauses are:

"17. Cargo is to be loaded, stowed and discharged by the charterers, free of expense to the vessel.

"18. Cargo is to be loaded, stowed and discharged within a total of twenty-three (23) weather working days of 24 hours, Sundays and holidays excepted unless used in which case actual time used to count. If longer detained charterers to pay demurrage at the rate stipulated in Clause 7 and payments to be made in the same currency of freight payment . . ."

Clause 7 in the original printed form quoted above was changed in the NICTRIC voyage charter by striking the old reference to "merchants" and inserting a

typewritten provision "Demurrage, if incurred, to be paid by charterers" so that Clause 7 in the charter in issue reads:

"7. Demurrage, if incurred, to be paid by charterers at the rate of Seven Hundred Dollars (\$700.00) per day or pro rata for any part of a day."

In these new typewritten provisions, twice repeated, once in Clause 7 and again in Clause 18, charterers (Schnitzer) assumed an unqualified obligation to pay demurrage. This is an obligation which did not exist in any form other than as a secondary liability under Clause 8, in the basic form of Gencon charter. The typewritten provisions expand and override the qualified obligation which was originally placed in the Gencon pattern.

This interpretation is further emphasized by the language provided in typewritten Clause 18 that payments of demurrage are "to be made in the same currency as freight payment." The typewritten language of Clause 1 of the NICTRIC charter relating to the rate of freight provides that the freight is to be paid in U. S. currency. Nowhere in its arguments does Schnitzer explain how receivers in Japan could be required to pay in U. S. currency.

Schnitzer also contends that it has avoided liability for the balance of freight (10%) which was agreed in the charter to be paid upon discharge. Schnitzer claims that the cesser clause likewise places the responsibility for the payment of this balance of freight upon the receivers, to be collected through the exercise of the lien.

However, here again the typewritten modifications of the basic Gencon form are inconsistent with the printed clause. The typewritten provisions found in the section of Clause 1 of the NICTRIC charter labelled "rate of freight" provide for "lumpsum" freight in U. S. currency, 90% to be prepaid and the balance payable upon completion of discharge. This type of an amendment is substituted for the original printing under which the owner was obligated to "deliver the cargo on being paid freight." This new typewritten clause making the balance of freight payable on completion of discharge, i.e., after the cargo has left the custody of the vessel, is totally inconsistent with owners looking first to a lien on the goods to pay the freight.

It is a fundamental rule of charter construction that the typewritten provisions take preference over the printed language. In *W. K. Niver Coal Co. v. Cheronea S. S. Co.*, 142 Fed. 402 (1st Cir. 1905), the Court held, at page 404:

"Charters, like nearly all maritime documents, can be properly construed only when construed historically. The common practice when changes have been desired in charters, marine insurance policies, and other maritime documents, has been to insert into the old body a new clause supposed to have reference to the particular emergency which it concerned. Thus, it follows that inconsistent expressions are found in such documents; and so it is in the present case. Scrutton's Charter Parties and Bills of Lading (5th Ed. 1904) at page 22, pertinently says: 'It is unnecessary to find a meaning in the particular charter for every word of a com-

mon printed form'. When a maritime document is studied historically, the necessity of complete reconciliation at time disappears, and what is introduced as new matter masters the rest of the document, on the same principle that written words master the rest of the printed blank deed, or contract, into which they have been inserted."

This same principle was followed by this Court in the *Robin Goodfellow*, 26 F.2d 343 (9th Cir. 1928) where the Court stated: (p. 344)

"The Court below held that decision depended upon the meaning of Clause 15 and Addenda C, and that, if there was a conflict between the two, the latter should control, for the reason that Clause 15 was in a printed form of the charter parties, while Addenda C was a typewritten clause attached thereto. . . . There can be no question but that the trial court properly held that, in case of conflict between the printed clause and the written clause appended to the charter parties, the latter must prevail. In so holding the Court followed a familiar rule of construction, which scarcely needs a citation of authority."

The trial court applied these principles (R. 139, 140) and held that the specific language in the typewritten additions was such that Schnitzer, without qualification, agreed to pay the demurrage. Schnitzer contends (Br. 39) that these changes in the original printed form do not alter the operation of the cesser clause.

Schnitzer claims that the trial court misinterpreted Clause 7 by taking one of the portions of it out of context. A comparison between the original printed lan-

guage of the Gencon form of Clause 7 and the one used in the NICTRIC charter party shows that the trial court did not take a portion out of context but that the typewritten changes completely altered the pattern set forth in the printed form. Clause 7 of the printed form, which was stricken, read:

“Ten running days on demurrage at the rate of \$..... per day or pro rata for any part of a day, payable day by day, to be allowed merchants altogether at ports of loading and discharging.”

As has been pointed out earlier, this printed language was consistent with the pattern of placing liability for demurrage upon the merchant receiver. However, in the NICTRIC voyage charter this pattern was changed by deleting it entirely and inserting:

“Demurrage if incurred to be paid by charterers at the rate of Seven Hundred Dollars (\$700.00) per day or pro rata for any part of a day.”

Schnitzer claims, at page 40 of its brief, that the function of Clause 7 is not to allocate liability for demurrage but to agree upon the rate at which demurrage would be paid. If that were so, Schnitzer could have merely inserted the rate in the printed Gencon form and the rate would have been agreed upon. Instead, it chose to modify the Gencon form completely and to make an unqualified agreement to pay demurrage if incurred..

Turning to Clause 18, Schnitzer contends this does not modify the allocation of liability for demurrage as set forth in Clause 8. No matter how Schnitzer invents argument, the clear language of Clause 18 does change

the allocation of liability. Clause 18, just as Clause 7, states categorically, and without any qualification, the obligation of "charterers to pay demurrage." Clause 18 further adds that payments of demurrage or dispatch are to be made in the same currency as the freight payment which, as pointed out above, is required to be in U. S. currency by Clause 1.

Clause 18 likewise makes it clear that no distinction can be drawn between demurrage incurred at the port of loading and at the port of discharging inasmuch as this clause provides that "cargo is to loaded, stowed and *discharged*. . . ." It then continues "if longer detained, charterers to pay demurrage at the rate stipulated in Clause 7. . . ." And Schnitzer agreed to be responsible for the discharge in Clause 17.

The cases cited by Schnitzer add nothing to its argument. The English trial court decision in "*Z*" *Steamship Co., Ltd. v. Amtorg, New York*, 61 Lloyds List LR 97, (K. B. Div. 1938) concerned a charter which contained none of the typewritten language which is crucial in this case. All it did was contain an unmodified Gencon printed Clause 8.

The arbitration in the *Luossa*, 1936 A.M.C. 213, held the unmodified Clause 8 to be effective because "no evidence was submitted or argument made that the clause was ineffective for any reason whatsoever." The additions made to the *Luossa* charter did not relate to the applicability of Clause 8.

Schnitzer next contends that there is no evidence that it was responsible for the language of the voyage

charter (Br. 42). The trial court finding on this point is (R. 140):

"The form of the contract, the language used, the deletions made and the endorsement attached are all chargeable to Schnitzer and I so find under the undisputed evidence before me. Therefore if ambiguity exists, which I do not believe, all doubt must be resolved against the author of the charter. *Thomas Jordan, Inc. v. Mayron Drilling Mud, Cam & Eng'r Serv.*, 214 F2d 410 (5th Cir. 1954)."

This finding is amply supported in the evidence.

Dr. Leonard Schnitzer stated that he handled the negotiations on behalf of Schnitzer (Tr. 174).

He did this through his broker, Seacharter. The testimony of Dr. Leonard Schnitzer (Tr. 177) clearly shows it was Schnitzer that directed the form of voyage charter. Dr. Schnitzer testified:

"I said 'Well' I said 'I've got another vessel'—I think it was the KEHREA—I said, 'This is a pretty uniform party and most of the standard conditions would apply in this particular case.' I said, '*If you want to use this as a form, on this basis we will pay \$63,000.00 and that is it.*' (Emphasis added)

In this negotiation there is no doubt that Seacharter Co., Inc. was acting as broker and agent for Schnitzer. This was the testimony of Mr. R. S. Kimberk in his deposition (Ex. 79). Although Schnitzer objected in the trial court to the admissibility of Mr. Kimberk's testimony, the objections were overruled and no error is assigned in this appeal based upon this ruling. Mr. Kimberk testified (p. 5):

"A. After the vessel had been chartered to Amtro Corporation, I had conversations with Mr. John Stewart of Amtro regarding his employment of that vessel. Following these conversations, I had further discussions with Mr. Jensen of Seacharter Company, Portland, with whom we were working on other business. He said he had arrangements with a firm in Portland whereby he could supply a cargo for the SS 'NICTRIC'.

Q. Mr. Kimberk, what was the name of this firm in Portland to which you referred?

A. Seacharter Company.

Q. And you stated that Seacharter had arrangement with a firm in Portland?

A. That's Schnitzer.

Q. Did Captain Jensen tell you what his connection was with Schnitzer?

A. He said that he was the exclusive agent for Schnitzer and had authority to arrange cargoes to be shipped by Schnitzer."

Mr. Kimberk testified concerning the beginning of negotiations to fix this charter and then confirmed that the final negotiations were conducted directly by Mr. Stewart, manager of Amtro.

The fact that Mr. Kimberk conducted the first part of the negotiations on behalf of Amtro was confirmed by Mr. Stewart (Tr. 34). On July 14, 1961 Seacharter sent Amtro a telegram setting forth the terms proposed for the charter (Ex. 51) as follows:

"Re various telephone conversations this morning your T/C vessel Nictric hereby accepted voyage charter to Schnitzer Steel Products under general Pacific Coast Scrap Charter Party with the fol-

lowing additional clauses one Port loading, one Port discharge, charterers option, loading Vancouver B. C. and/or Portland to one or more discharge Ports Kobe/Osaka, Tokyo/Yokohama. \$2500.00 additional each loading and discharge port charterers option loading and discharge in or out of geographical rotation charterers option loading 1500 tons Turnings. Lay Days August 18 Sept. 3. Total Brokerage 3-3/4 percent your guidance mailing today sample Charter Party. Mailing Monday complete written Charter Party for your acceptance.

Capt. John L. Jensen, Seacharter Co., Inc."

Subsequently, Seacharter wrote to Amtro enclosing a copy of the form used for the charter of the KEHREA (Ex. 76), the one mentioned in Dr. Schnitzer's testimony (Tr. 177).

Mr. Stewart further testified that upon receipt of the form of charter, he discussed the matter with Captain Jensen of Seacharter objecting to the form submitted (Tr. 37). But this was of no avail. Mr. Stewart testified he thereafter discussed his objections with one of the Schnitzer brothers whom he believed to be Morris Schnitzer. It was made quite clear by Dr. Leonard Schnitzer that if Amtro did not give them the vessel on his terms there was going to be a lawsuit, because he considered it chartered and fixed (Tr. 181).

Thus, the factual situation presented to the trial court showed that Schnitzer directed its agent, Seacharter to utilize the KEHREA form of charter. This form was utilized by Seacharter and sent to Amtro. When Amtro objected to the form of the charter,

Schnitzer threatened litigation if it were not promptly executed. This clear evidence amply justified the trial court's finding that "The form of the contract, the language used, the deletions made and the endorsement attached are all chargeable to Schnitzer and I so find under the undisputed evidence before me."

Schnitzer's claim that there is no evidence upon this point as raised in its brief at page 42 is completely without foundation.

Schnitzer next contends there is no evidence that Schnitzer agreed with the court's construction of the voyage charter (Br. 42).

The court's findings on this point are as follows (R. 140):

"Aside from the views here expressed on the interpretation of the charter, I find a record which places Schnitzer in the indefensible position of first agreeing to pay demurrage, and later attempting to change its position. On November 13, 1961 when Schnitzer was first contacted by Amtro's counsel after the vessel had been on demurrage for about one month, Schnitzer agreed to pay demurrage, but objected to payment of that item and the balance of the freight until the completion of the discharge, on the ground that such items were not due under the charter until that time. This testimony of a Mr. Fletcher is uncontradicted. Subsequently, Schnitzer's counsel took the position that in fact there was no lien on the cargo for the demurrage. Schnitzer relied on this construction of the contract from about November 17th until after the cargo

had been discharged on December 31st. On December 7th, counsel advised Amtro that it would not comply with what Amtro thought was a firm agreement to pay a portion of the demurrage and arbitrate the disputed amounts. At this time Amtro was advised to take whatever remedies it thought it might have. On December 11th, Amtro advised Schnitzer that it probably could not exercise a lien on the cargo on account of Japan's peculiar laws and of the fact that considerable of the cargo had been discharged. On December 14th, by the libel in this case Owners advised Schnitzer that they had been unable to obtain payment of the demurrage by exercising a lien on the cargo. Until December 7th, it is quite clear that Schnitzer interpreted the contract in line with Amtro's and this Court's conclusions. A cable on August 11th indicated such an interpretation. A letter to Amtro on August 27th applied the same construction. One week later in an inter-office memo to its Tokyo office, Schnitzer conformed to this same interpretation. The record clearly shows that the indicated 'small fortune' was the sum being lost on demurrage. On all contracts with purchasers at the ports of discharge, the demurrage is for the sellers, i.e., Schnitzer's account with one exception. At Okaya, one purchaser agreed to pay his proportionate share of demurrage."

The record amply supports these findings. Mr. Fletcher testified (Tr. 104) as follows:

"The response I got from that cable or telegram was a telephone call on November 13, 1961. It was a telephone call in which I talked to Dr. Leonard Schnitzer and Kenneth Lewis. I believe that one or

the other of them placed the call but both of them were on the telephone. We talked about the cable. They told me they were going to pay the demurrage, but that the demurrage was not yet due; that the provision for payment of the demurrage day by day in the charter was crossed out, and that the balance of freight was not payable until the completion of discharge, and that the demurrage is treated the same way and that the demurrage was not due; that they were going to pay it but they were unwilling to prepay it."

The court found that Schnitzer's counsel took the same position. Mr. Fletcher (R. 107) testified:

"On the same day (November 17) Mr. Krause called me, or I called him—I don't recall—and we discussed the situation at some length. We discussed the problem in a series of telephone conversations, conversations between the 17th and the 27th. And during all of these conversations Mr. Krause told me that he had examined the charter; that I would notice that the provision for demurrage payable day by day had been crossed out; that I would notice, also, that the charter provided for the balance of freight payable after completion of discharge; that in his view demurrage was simply extended freight, and that, therefore, demurrage was not payable until the completion of discharge; and that if the bill was not payable until the completion of discharge we had no lien because you don't have a lien for something which is not yet due."

This testimony of Mr. Fletcher was never contradicted.

It is uncontradicted that on November 29 Schnitzer's counsel advised Amtro that he had been authorized by his client to accept the proposal which the attorneys had been discussing, namely, the payment of the demurrage except for Sundays and holidays and the arbitration of Sundays and holidays (Tr. 109).

This was further confirmed by Mr. Fletcher's testimony that on December 5 Mr. Fletcher was told by Schnitzer's counsel that he had talked to his client about the agreement and that it would be signed and the funds would be on their way immediately (Tr. 113).

It was not until December 7th that Schnitzer's counsel informed Amtro that Schnitzer was not going to go through with the agreement (Tr. 113).

But the negotiations did not end then. Mr. Lewis, Schnitzer's general counsel, went to Los Angeles on December 11th in an effort to settle the demurrage issue again. But Schnitzer and Amtro were unable to agree on the amount. It is clear that Mr. Lewis' visit to Los Angeles in no way questioned Schnitzer's liability for the demurrage but was merely haggling over the amount to be paid (Tr. 114, 115).

On December 12 Mr. Fletcher advised Mr. Lewis that his information was that it was impossible to exercise the lien at which point no further negotiations or discussions were promoted by Schnitzer (Tr. 115, 116).

Not only was Schnitzer indicating that it considered itself liable for demurrage throughout the negotiations covered in the testimony above, but Schnitzer had ear-

lier confirmed this interpretation in communicating with Amtro and with Schnitzer's Japanese office. This is contained in Exhibits 49, 53 and 54 as follows:

"... EXTREMELY CONCERNED ABOUT NIC-
TRIC DEMURRAGE AT YOUR END AS THIS
VESSEL WILL DISCHARGE OSAKA/TOKYO
BOTH IF DELAYED BOTH PLACES WE
COULD HAVE TREMENDOUS DEMURRAGE
BILL WHAT IS OUTLOOK ON DEMURRAGE
FOR THIS VESSEL ADVISE IMMEDIATELY
..."

(August 11, 1961 to Schnitzer Tokyo office) (Ex. 49)

"We have been losing heavily on several of our vessels because of these delays, and needless to say, we are as anxious as you to complete same."

(October 17, 1961 letter to Amtro) (Ex. 53)

"4. Also, enclosed find photostatic copy of letter from AMTRO corporation, received earlier this week. These people are hotter than the dickens because they have to book a return cargo on the NICTRIC, and they don't know when we will finish discharging. They have to synchronize the loading of their cargo to our discharge of the vessel. When will the vessel go to berth? When will it finish discharging? We are losing a small fortune on this vessel. Would appreciate some answers. Anything you can do to expedite the matter will be of tremendous help."

(October 25, 1961 to Schnitzer's Tokyo office) (Ex. 54)

In the interoffice memo to its Japanese office (Ex. 53) Schnitzer indicated concern with "losing a small fortune on this vessel." The testimony of Dr. Leonard Schnitzer (Tr. 207-209) makes it abundantly clear that this "small fortune" was the sum being lost on demurrage, and it was so found by the trial court (R. 140).

Schnitzer's brief upon this point (Br. 42-46) makes no attempt to explain any of the above testimony but seeks to ignore it.

Instead, Schnitzer attempts to avoid the District Court finding of "a record which places Schnitzer in the indefensible position of first agreeing to pay demurrage, and later attempting to change its position" by pointing its finger at Amtro. Of course, Amtro in its desperate financial condition had no alternative available to obtain demurrage payments than to threaten to lien the cargo and such threats were made. But in answer to these threats, Schnitzer continued its position that it would pay the demurrage but that these sums were not yet due. This placed Amtro in a helpless posture and it became insolvent.

Schnitzer proceeds with its argument that Amtro's counsel consistently claimed the lien during his discussions with Schnitzer until it was clear that a lien could not be imposed on December 11. What Schnitzer does not quote in its argument is the uncontradicted testimony of Mr. Fletcher set forth above that Schnitzer was at all times agreeing to pay demurrage but objecting to payment of that item until the completion of discharge. At page 46 of its brief Schnitzer states

"Schnitzer never took the position that Amtro had no lien on the cargo." The uncontradicted testimony on this point appears in Mr. Fletcher's testimony (Tr. 107) and quoted above, and this uncontradicted testimony was accepted by the court.

The pleadings and the pre-trial order not only asserted the inability to obtain payment of the demurrage by exercising a lien on the cargo but also asserted Schnitzer's primary liability under the terms of the voyage charter (R. 5, Art. XVI; R. 16, par. IV; R. 39, Art. XV; R. 109, par. 9; R. 110, par. 2, 3, 4).

And the same contention is made in Paragraph IX which is:

"IX. Under the terms of said voyage charter and in light of the circumstances then prevailing in the ports of Japan at the time said vessel was awaiting discharge and discharging Schnitzer remained liable to pay any and all demurrage which accrued." (Italics added)

These pretrial contentions on behalf of Owners quite clearly pleaded alternative relief, in the first instance alleging that Schnitzer was liable under the terms of the voyage charter and second, that in any event, it was impossible to exercise a lien upon this cargo under the circumstances then prevailing in Japan.

Schnitzer's final attack upon the trial court's interpretation of the voyage charter is upon the court's finding that the contracts between Schnitzer and its customers placed the responsibility upon Schnitzer for demurrage (R. 142, Br. 47).

Schnitzer mistakes the trial court's finding on this point. It claims the court found that all of Schnitzer's contracts for sale of cargo, with one exception, provided that liability for demurrage at the unloading port, as between Schnitzer and its buyers, was upon Schnitzer (S. Br. 47).

The Court's finding was (R. 142):

"On all contracts with purchasers at the ports of discharge, the demurrage was for the seller's, i.e., Schnitzer's account, with one exception. At Okaya, one purchaser agreed to pay his proportionate share of demurrage."

What the Court found was that in only one contract (Okaya) (Ex. 112) did Schnitzer shift its burden of paying demurrage. The provisions of the Okaya contract (Ex. 112) spell out in considerable detail the demurrage obligation of the buyer.

"5. DELIVERY: C & F Free Out Tokyo, Japan
Buyer shall discharge at the rate of 150 long tons per workable hatch per WWSHEX, even if used. Waiting time of the vessel at discharging port shall be shared by us proportionally according to our invoice tonnage and total quantity. Time to count from 8:00 a.m. the following working day after due notice given; Notice of readiness to be given in writing during office hours. Time from noon Saturday to 8:00 a.m. Monday not to count, even if used. Any demurrage or despatch money according to the above calculation shall be for Buyer's account. Rate of demurrage/despatch to be \$700—per day and half despatch."

The obligation assumed by Okaya is not the same as the charter terms in calculation of lay time, use of Saturdays and Sundays and despatch money, so that the application of the voyage charter calculations might result in an entirely different sum than what Okaya agreed to pay.

The Court's finding on this point is consistent with the other findings relating to Schnitzer's course of conduct interpreting the voyage charter to place the responsibility for demurrage upon Schnitzer. Had Schnitzer not realized its responsibility for demurrage, it would not have made the contract with Okaya in those terms.

The remaining contracts Schnitzer had with its customers were similar. The contract with Toyo Menka Kaisha, Ltd. (Ex. 16) contained this language:

"(7) Discharging: Discharging shall be made by Buyer for Buyer's account. Buyer guarantees customary quick despatch (C.Q.D.)."

It also contained as a price provision, C&F FO. When Dodwell & Co made demand upon this purchaser to pay demurrage (Deposition Ex. F-1) this customer replied (Deposition Ex. F-2):

"In reply to your letter of November 27, 1961 concerning the payment of demurrage and freight on the captioned vessel, we would inform you that we bought our cargo from our shipper on the terms of C&F FO, which means that we have nothing to do with freight or demurrage.

"Under the circumstances we regret we cannot take any action as requested."

The Mitsui contracts (Ex. 18, 19) were even clearer. They provided:

"Unloading

CQD (Liner term discharges except stevedoring charges are for buyer's a/c), therefore demurrage at discharging port is for seller's a/c."

Both of the Mitsui contracts were CIF FO Tokyo. Mitsui likewise rejected the proposal made by Dodwell (Deposition Ex. F-3).

All of the remaining contracts called for CIF FO with the exception of the Kuwamasi contract (Ex. 110, which, in addition, called for "Berth Terms."

Schnitzer argues that because the contracts place the burden of paying for the discharge on the buyer, this, in some manner, places the burden for demurrage also upon the buyer. No authority is cited on this point and the evidence quoted above is to the contrary.

The only obligation which a consignee assumes is to use reasonable diligence under the circumstances then prevailing. See Scrutton on Charter Parties (16th Ed.) p. 309:

"The obligation, therefore, upon the charterer or consignee, where no fixed time for discharge is mentioned, is in all cases, that the ship is to be discharged as quickly as is consistent with the manner in which every vessel going to the port is discharged, and the existing circumstances at the time when the vessel actually comes to the port, so far as these circumstances are not caused by the charterer or consignee. It follows, that, with such an obligation in a charter party or bill of lading there

is no advantage in inserting exceptions affecting the obligations as to discharge though this is commonly done."

Schnitzer then argues that the inclusion of reference to the voyage charter in the bills of lading shifted the liability for demurrage to these customers. This is merely a re-argument of Schnitzer's first point on interpreting the voyage charter. As has been discussed above, the language of the voyage charter squarely places responsibility for demurrage upon Schnitzer. How could the incorporation into the bills of lading of Schnitzer's obligation for demurrage in any manner transfer that obligation to the customer? Obviously, it could not and Schnitzer, in only one of its contracts, expressly shifted this responsibility to its customer (*Okaya Ex. 112*).

Further, these contracts with the customers called for bills of lading marked "freight prepaid." Did Schnitzer want the vessel to lien the cargo for the unpaid freight under such circumstances? Clearly not, and the trial court properly held that Schnitzer's manner of handling its customers contracts was in accord with the interpretation of the voyage charter made by the court.

In summary upon Point I of Schnitzer's argument, an objective analysis of the voyage charter can lead to but one conclusion—that Schnitzer agreed, without qualification or ambiguity, to pay any demurrage which might be incurred under the voyage charter. Schnitzer, by its actions from the inception of the charter until the vessel was completely discharged, acted in accordance with this interpretation that it was responsible for de-

murrage but the demurrage was not payable until the discharge was completed. Schnitzer is fully chargeable with the authorship of the terms of the voyage charter and should there be any ambiguity, which neither the court nor either of the other parties believe, such ambiguity should be resolved against Schnitzer. And finally, in its contracts with its customers and its dealings with its customers, Schnitzer recognized its responsibility for payment of the demurrage and balance of unpaid freight.

The District Court so found, based upon substantial evidence and should be affirmed.

II

ANSWER TO SCHNITZER'S GROUP II ARGUMENT

The Lien on Cargo Could Not Have Been Exercised.

The correct interpretation of the voyage charter made by the trial court disposes of the issue of Schnitzer's liability for demurrage and unpaid freight. But, despite this, even under Schnitzer's theory of the case, Schnitzer remained liable under the cesser clause (Clause 8) because the parties were unable to obtain payment of the unloading demurrage by exercising a lien on the cargo. The trial court took into account every proposition advanced by Schnitzer and held that a lien could not have been so exercised.

The District Court held (R. 142) that "Schnitzer's argument that Amtro made no attempt to enforce payment of the demurrage by exercising a lien is simply without foundation."

There is no dispute on the incredible congestion in Tokyo which caused the delay of the NICTRIC. As Captain Cassimatis testified (Ex. 47, p. 20):

"A. Well, it was a well-known fact throughout the shipping fraternity that the congestion of '61 never happened in the annals of Japan. There must have been around 300 ships at the time all over Japan staying between four months down to two months and even grain ships had to be delayed which always get preference.

Q. Was it the worst congestion you have ever seen in your shipping career?

A. That is correct.

Q. And the worst you ever heard about?

A. The worst I ever heard and the worst a lot of people with perhaps more experience than myself have ever seen or heard in Japan."

The Agency Japan Newsletter No. 2 published by PacMarine (Ex. F-23) also brings this out. At page 1, the heading of the Newsletter is:

"While there are many items of interest to ship-owners and charterers to maintain this newsletter with general subjects, at the present time the single subject of paramount interest and importance to all concerned is that of CONGESTION, and we think it worthwhile to devote this issue solely to this one subject."

And at page 3:

"II. Present Position:

A) Degree of Congestion:

5) Tramp vessels discharging lumber, logs (into the water) or scrap into 'dirty cargo' lighters—great congestion ranging

from one week to three months' wait for berth and three weeks to one and one-half months for discharge."

And at page 4, under the heading of Causes:

"The main cause is the tremendous increase in the import of bulk commodities mentioned above.

The other more local causes are as follows:

- a) Shortage of berths
- b) Shortage of lighters
- c) Shortage of warehouse space
- d) Shortage of labor"

With reference to these shortages, the report continues (p. 5):

"(b) Lighters—Here we have a bad bottleneck, in that there are two types of lighters—clean cargo lighters for general cargo, import and export, grain, sugar, etc. Generally while these are short it is not catastrophic. The other—dirty cargo lighters are extremely short, partly in their own right and partly because of lack of areas into which they can discharge, causing much slower turnaround. The Government calculates that the ports are short of 250,000 tons of lighters, of which 60,000 each are in Tokyo and Yokohama.

(c) Warehouses—This business has been an excellent one since the war; space is normally short but now with the great splurge, the warehouses are pack-jammed, with shortage of labor to clear them and as a result cargo remains in lighters for undue time causing a snowballing effect. Shippers and consignees who usually use their own private warehouses now have them full with import cargo and have to use port warehouses which compounds the problem."

Schnitzer does not deny this incredible congestion. Instead, it attempts to misconstrue or belittle the testimony to argue that nothing was done to enforce a lien.

Under general maritime law, the lien of a vessel on cargo for freight and demurrage is possessory and is lost when the cargo is delivered to the consignees. *Bags of Linseed*, 17 L. Ed. 35; *Riley v. Cargo of Iron Pipes*, 40 Fed. 605; *The Guilio*, 34 Fed. 909; *Pioneer Fuel Co. v. McBrier*, 84 Fed. 495; *Costello v. Laths*, 44 Fed. 105; *In Re Bags of Malt*, 262 Fed. 946. Under this principle, to effect a lien upon the cargo, the vessel would have had to retain possession of the scrap, either in warehouse space ashore, on the lighter or on the ship itself.

The overwhelming evidence is that there was no warehouse space available, there were no lighters available, and that should the vessel attempt to keep the cargo aboard, it would have been ordered out of its turn at the buoy and placed again at the end of the line of ships awaiting their turn to discharge. See testimony of Main (Ex. 44G, p. 153, 154, 173), Saishoji (Ex. 44E, p. 23, 24, 25, 35, 57-59), Cassimatis (Ex. 47, p. 18-20, 53, 60).

It was simply not possible under the conditions then prevailing in Japan to exercise the lien. As Mr. Main testified (Ex. 44G, p. 173):

“L.: Yes certainly. I want to know why you say it’s not possible.

“M.: Well, I say it was not possible because there was no storage space ashore, and, nor could we get barges to hold it in the barges or the lighters.”

Schnitzer treats the testimony from Japan with all the technical niceties possible. Voluminous objections were presented to the trial court (R. 123) and patiently considered and disposed of (R. 184). In considering these objections the District Court had in mind the familiar admiralty practice. See Benedict on Admiralty, § 381 (b):

‘Admiralty causes are tried by a single judge, without the aid of a jury. Hence the elaborate rules of evidence deemed necessary to protect the untrained jury are not required. Courts of admiralty are not bound by all the rules of evidence which are applied in court of common law and they may, where justice requires it, take notice of matters not strictly proved and may receive in evidence testimony which might not be admissible in other courts.’

See also, *Waterman Steamship Corporation v. David*, 353 F.2d 660 (5th Cir., 1965); the *Denny*, 127 F.2d 404 (3rd Cir., 1942); *Westchester Fire Ins. Co. v. Buffalo H. & Salvage Co.*, 40 F. Supp. 378 (D.C. W.D. N.Y. 1941).

The testimony shows that Dodwell was, without doubt, the most experienced agent in Japan and handled by far the great majority of the vessels having delay and demurrage problems (Ex. 44G, p. 156, 157). It knew the practical day-to-day operational problems being encountered during this congestion. Dodwell’s men testified that, based upon their expert knowledge of the conditions then existing in Tokyo, it was physically impossible to assert a lien upon this cargo by any of the

three methods suggested above for retention of a possessory lien (Ex. 44G, p. 161) (Ex. 44E, p. 140).

Not only did Dodwell so conclude, but also experienced maritime counsel in Japan likewise advised that it was not possible to exercise a lien under the conditions then present (Ex. 47, pp. 19, 48, 50, 60).

In summary, the owners' managing superintendent was personally present in Japan with his own observation of the tremendous congestion. The best and most experienced steamship agents in Japan were watching out for the vessel's interest to protect its demurrage claim. And the maritime attorneys, who for so long had looked after such matters for vessels of all nations, were consulted. All agreed it was impossible to exercise the lien. And the trial court so found.

Schnitzer stopped its negotiations with Amtro immediately when it learned that a lien could not be exercised. Mr. Lewis was so told by Mr. Fletcher. The original libel herein was filed on December 14, 1961 before all of the cargo had been removed.

Had Schnitzer honestly felt a lien could have been exercised, or had Schnitzer wanted to fix the demurrage expense upon the cargo receivers, why did Schnitzer not come forward with all the suggestions it made to the trial court, and now repeats to this Court, before the cargo was completely unloaded? Why did it not say "Keep some cargo aboard," or "Go to Harumi Wharf," or suggest some bonded storage areas? Schnitzer not only had an office and personal representative in Japan, but it also had appointed the vessel's agent, Pac-

Marine. If the knowledge of PacMarine was superior to that of Dodwell and had Schnitzer wanted to place this liability upon its customers, why was this superior information not given to Amtro, especially as PacMarine was supposed to be agent for both Schnitzer and Amtro? The only answer is that Schnitzer was not interested in placing this liability upon its customers. When it learned of the congestion and the impossibility of exercising the lien, Schnitzer saw the situation as an opportunity of avoiding the demurrage claims entirely.

Turning to Schnitzer's specific suggestions of how the lien could have been exercised, the trial court found that the idea of retaining some cargo on board was not practical (R. 142). It held that the ship risked not only the possibility, but also the probability of being moved by the harbor authorities and sent to anchor outside to await another turn at discharge. This would further delay the ship for an indefinite period to such an extent that no one could predict what the ultimate demurrage bill would be. Both Main (Ex. 44G, p. 160) and Saishoji (Ex. 44E, pp. 24-25, 57-59) testified that the ship would undoubtedly have been forced to move from its discharging buoy if it had attempted to exercise its lien by stopping discharge. All Schnitzer does is argue that it should have been tried to see what would happen. Common sense alone dictates that the harbor authorities in Japan would not have permitted an idle ship to hold up the long line of waiting vessels.

Schnitzer challenges the ruling of the District Court that the NICTRIC could have been moved to another

wharf and the lien exercised there (R. 143). This was referred to as the Harumi wharf. Schnitzer's own witness, Koizumi of PacMarine (Ex. 44H), provides evidentiary support for this finding against Schnitzer's claim. This man was acting under Schnitzer's appointment as its agent (Ex. 44H, pp. 187-8) and testified on this point (Ex. 44H, p. 187-11):

"B: What about the Harumi wharf that you have been talking about why didn't you make an effort to engage that wharf?

"K: We couldn't do that.

"B: Why not?

"K: The reason is because we couldn't discharge in seven days. I mean on the whole cargo I am talking about."

He never made any effort to put the vessel at Harumi wharf (Ex. 44H, p. 187-18).

Ex. B-11 produced in Morgan's deposition (Ex. 44F, p. 89) is consistent with this testimony of Koizumi. Morgan wrote (Ex. B-11, p. 1):

"During my visit to Tokyo in the period 21st October to 8th November, Schnitzer Steel Products' Tokyo representative, Mr. Morgulis, had been endeavoring to arrange for the NICTRIC to discharge out of turn at a special quick discharge berth, but subsequently gave up the idea because of the NICTRIC's varied types of scrap cargo which would not admit of completion within seven days."

This is a statement attributed to Schnitzer's admitted agent, Morgulis, and certainly is not hearsay against Schnitzer. Morgulis was present at the depositions in

Japan (Ex. 44D, p. 34) and could have denied that statement attributed to him had it been untrue. Morgulis, significantly, was not called as a witness by Schnitzer.

Schnitzer also challenges the District Court's finding that there were no areas ashore where the scrap could have been stored (R. 143). The complete lack of such storage facilities was told by Main (Ex. 44G, pp. 153-4, 173) and Saishoji (Ex. 44E, p. 23). Only Koizumi in response to hypothetical questions felt he could have found some space ashore. But Koizumi's testimony on this point also is suspect for two reasons—(a) he was the agent of the vessel at the time of discharge and did not suggest any such areas at the time, and (b) his own company's reports (Ex. F-23) quite clearly stated there was no space ashore.

Schnitzer objects to Ex. F-23, but its own witness Koizumi said the report was put together by his company as the best information it had based on matters with which it dealt daily (Ex. 44H, p. 187-24, 25). If for no other purpose it was admissible to impeach Koizumi's direct testimony. It was also a normal business trade information bulletin designed to inform people of the actual conditions (Ex. 44H, p. 187-24).

All of the "possibilities" suggested by Schnitzer in its hypothetical questions to Koizumi and its arguments are thus demonstrably false and implausible. The District Court so ruled.

Schnitzer challenges the Court's finding that the Japanese statutory lien could not have been exercised

because delivery had been made to third party purchasers from the consignees and not to the consignees (R. 143). It is Schnitzer's contention the Japanese law permits a shipowner to pursue the goods in the hands of a consignee for a period of two weeks after delivery (Br. 71). That, however, was impossible here because delivery was made directly to third parties. See testimony of Yoshida (Ex. 44B), Kayashima (Ex. 44C) and Haya-shibara (Ex. 44D).

The exhibits produced at the trial further show that these deliveries were made to other than the consignees named in the bills of lading. These outturn survey reports show, in every instance, that at the time of inspection all of the scrap was in the hands of third parties and not in the hand of consignees. These outturn survey reports are as follows:

Exhibit #23 Japanese survey—Iwai discharge

“(b) Place and date of inspection:

At the landing place of Tokyo Steel Mfg. Co., Ltd.,
Tokyo on Dec. 30, 1961

“Consignee: Iwai

Consumer: Tokyo Steel Manufacturing Co., Ltd.”

Exhibit #24A Japanese survey—Toyo Menka discharge

“(b) Place and date of inspection:

At the landing places of Fuji Shokai K. K., Shibaura & Shinonome, Tokyo on Jan. 6 and 9, 1962

“Consignee: Toyo Menka

Consumer: Fuji Shokai K. K.”

Exhibit #24 B Japanese survey—Toyo Menka discharge

“(b) Place and date of inspection:

At the landing places of Harumi, Shibaura and consumers' yards in Tokyo on Dec. 9, 1961 and subsequent dates

“Consignee: Toyo Menka

Consumer: Fuji Shokai K. K.”

Exhibit #25 Japanese survey—Okaya discharge

“(b) Place and date of inspection:

At the Toyohashi Works of the Tohto Seiko Kaisha, Ltd., on November 20, 1961 and subsequent dates.”

“Consignee: Okaya

Consumers: Tohto Seiko Kaisha, Ltd.”

Exhibit #26 Japanese survey—Mitsui

“(b) Place and date of inspection:

At the loading place of Harumi, Tokyo and consumers' yard Kawaguchi Saitama Pref. on Dec. 6, 1961 and subsequent dates:

“Consignee: Mitsui

Consumers: Messrs.—Nakadaya Shoten

Kogai Kogyo K. K.”

Exhibit #27 Same as Exhibit #26 above

Exhibit #29 Far East Superintendency Co., Ltd.,
Surveyer—Namura Trading Co., Ltd.—New America
discharge

“This is to certify that we attended at Tokyo port
on December 23, 24, 25, 27, 28 and 29, 1961 and

at the premises of Asahi Sanbashi, of Suzue Gumi Warehouse, Harumi, Tokyo, and at the receivers' premises in Kawaguchi on December 27, 28, 29 and 30, 1961 and on January 6, 7 and 8, 1962, for the purposes of viewing the discharge landing and weighing and inspecting the following:"

Schnitzer argues that these outturn survey reports are not evidence of the passing of title. This is not the point. The evidence introduced by Schnitzer of Japanese law is that the lien may be pursued if the goods are in the hands of the consignee. These outturn reports show that the goods were not in the hands of the consignee but were in the hands of third parties.

In continuing the challenges to every ruling made by the District Court, Schnitzer complains of the decision that Amtro was not in a position to effectively assert its lien on account of the representation of Schnitzer that the demurrage and unpaid freight would be paid.

Owners take the position that the facts discussed above show quite conclusively that payment of the demurrage could not be obtained by exercising a lien on the cargo. Regardless of the representations made by Schnitzer to Amtro, the lien simply could not have been exercised under the circumstances then prevailing in Japan.

Had the circumstances in Japan been different so that a lien could have been effectively asserted, Schnitzer's representations were such as to place Amtro in an untenable position. And this was the finding of the trial court as an additional reason for holding Schnitzer liable for the demurrage and unpaid freight.

The uncontradicted testimony of Mr. Fletcher is (Tr. 104-105):

"They (Schnitzer) told me that they were going to pay the demurrage, but that the demurrage was not yet due . . . and that the balance of freight was not payable until the completion of discharge, and that the demurrage was treated the same way and that the demurrage was not due; that they were going to pay it, but they were unwilling to pre-pay it. I told them that we had to have some guarantee for this payment if we were not to go ahead with the lien. They said they would guarantee it."

And again (Tr. 107):

"And during all of these conversations Mr. Krause told me that he had examined the charter; that I would notice that the provision for demurrage payable day by day had been crossed out; that I would notice, also, that the charter provided for the balance of freight payable after the completion of discharge; that in his view the demurrage was simply extended freight, and that, therefore, demurrage was not payable until the completion of discharge; and that if the bill was not payable until the completion of discharge we had no lien because you don't have a lien for something which is not yet due."

In its brief, Schnitzer misconstrues the testimony of Mr. Fletcher (Tr. 113) in which Mr. Fletcher quoted Mr. Krause stating that his clients were not going to go through with the agreement. This was the agreement described earlier by Mr. Fletcher as the agreement to pay demurrage except for Sundays and holidays (Tr. 109).

Mr. Krause did not, as Schnitzer claims in its brief, decline responsibility. This is further supported by Mr. Lewis' trip to Los Angeles on December 11 and the continued negotiation between Amtro and Schnitzer at that point. This is further amplified clearly in Mr. Krause' letter (Ex. 34) taking the position that no lien could be asserted against the cargo and that nothing was due by way of demurrage or unpaid freight prior to discharge of the vessel.

It was not until December 29 that Schnitzer denied all liability for demurrage and freight as shown on Exhibit 61.

With this state of the record the court quite properly concluded that Amtro was not in a position to effectively assert its lien on account of the representations of Schnitzer that the demurrage and unpaid freight would be paid.

In summary upon this point, Owners submit the trial court was fully supported in its conclusion that even if Clause 8 remained in full force and effect, not modified by the typewritten language, the lien could not have been exercised in Japan under the circumstances then prevailing. Owner's had their marine superintendent personally present in Japan. The best and most experienced steamship agents were watching out to protect the demurrage claim. Maritime attorneys in Japan were consulted. All agreed it was not possible to exercise the lien. Only Koizumi provided some speculative possibilities, but none of the possibilities was given to Amtro or Owners when the NICTRIC was in Japan.

III

ANSWER TO SCHNITZER'S POINT III

Once on Demurrage, the Demurrage Runs Continuously

Schnitzer's third point on appeal is that the trial court rejected Schnitzer's contention that the time from noon Saturday until 8 a.m. Monday should be excluded from the calculation of the demurrage. The court's holding is clearly in accord with the law, and Schnitzer cites no authorities in opposition. The leading case is *Berwind-White Coal Mining Co. v. Solleveld, etc.*, 11 F.2d 80 (4th Cir. 1926), in which the Court said:

"As to the first proposition, the rule is that, after demurrage has commenced to run, it will not be suspended by the occurrence of an event within the exceptions of the loading cause. *Washington Marine Co. v. Rainier Mill & Lumber Co.* (D. C.) 198 F. 142; *The Oluf* (C. C.) 19 F. 459; *Lindsay v. Cusimano* (C. C.) 12 F. 504; *James v. Brophy*, 71 F. 310, 18 C. C. A. 49; *Baldwin v. Sullivan*, 36 N. E. 1060, 142 N. Y. 279; *Uulster Brick Co. v. Murtha*, 154 N. Y. S. 834, 169 App. Div. 151; *Scrutton on Charter Parties and Bills of Lading* (11th Ed.) 342; *Poor on Charter Parties* 349; *Carver, Carriage by Sea* (5th Ed.) 258c. In *MacLachlan's Law of Merchant Shipping* (5th Ed.) p. 589, it is said: 'Unless the contrary be clearly stipulated, time runs continuously for the payment of demurrage without regard to day or night or nonworking days.' "

This is also the position of the leading American text on the subject—*Poor on Charter Parties and Ocean Bills of Lading*, § 49, p. 118, in which the author states:

"Once the laydays have expired, and the ship is on demurrage, the demurrage days run continuously. The exception of Sundays, holidays, strikes, etc. is no longer of any value. This is for the reason that the charterer is considered as having failed in his duty by not having loaded the ship in the layday."

As has been pointed out above, the trial court was correct in attributing the authorship of the form of the voyage charter to Schnitzer so that if there is any ambiguity, which Owners contend there is not, the ambiguity must be resolved against Schnitzer. There is no clear stipulation that weekends should be excluded from demurrage contrary to the established practice of the shipping business and contrary to the authorities quoted above.

IV

ANSWER TO AMTRO'S POINT III

Trial Court Properly Construed Clause 23 of Time Charter Relating to Crew Overtime

The District Court construed Clause 23 of the time charter (R. 133-134) to mean that the parties intended a flat \$350 per month, or pro rata for a partial month, regardless of the actual amount of overtime consumed. This finding was based upon an analysis of Clause 23 in its original printed form and as it was changed by interlineation, together with the testimony of Captain Cassimatis, the only witness who discussed this point.

As the District Court said, it is of vital significance that the parties eliminated the printed language which

read "Officers, engineers, winchmen, deckhands and donkeymen for overtime work done in accordance with the working hours and rates stated in the ship's articles." In lieu of that language, the parties agreed that the charterer would pay "\$350 per month or pro rata in lieu of all overtime."

The interpretation urged by Amtro of the foregoing language is that the overtime sum should be calculated only during the periods of loading and discharge. Should this interpretation be correct, then there would have been no necessity for the parties to eliminate the printed language and substitute the new language.

The reason for this amendment to Clause 23 and its development in the field of chartering were explained by Captain Cassimatis in his deposition (Ex 47, pp. 12-16). Captain Cassimatis' qualifications in this field were not disputed, and he testified (Ex. 47, p. 12):

"Now, to us it was a question of sometimes the captains wanted to charge more overtime or some of the mates would charge more overtime, and some of the time charterers were a bit stingy and they were arguing about the amount of overtime presented, so somebody thought to make it in a lump sum; and it must be about five or six years, perhaps ten years, no more, that somebody thought of this practice of a lump sum, and since then most of the time charter, charter parties, express the overtime in a lump sum and avoid all this argument about the hours and about whether it was due or whether it was not due.

Q. Now, under the old form that you described was it necessary to make an actual accounting of

the overtime that was actually worked?

A. Actual accounting, yes, sir.

Q. And then settle that between the time charterers and the others?

A. That's right. You had to write everything, the time, the kind of work, the nature of the work, and all sorts of things.

Q. So to avoid that, this clause was devised to in effect settle in advance that argument?

A. Settle in advance, yes, sir.

Q. So that instead of computing the actual overtime a lump sum of so much per month was agreed upon?

A. That is correct.

Q. Whether overtime was worked or not?

A. That is correct."

This testimony of Captain Cassimatis was not challenged by any testimony or exhibits by Amtro, but only by argument. Thus, his testimony stands undisputed and is in accord with the change made by the parties from the printed language of the time charter to the interlineation as pointed out above.

In its brief, Amtro repeats its contention that the \$350 per month payment is applicable only during periods of loading and discharge and merely substitutes the sum of \$350 per month, or pro rata, for the actual hourly rates of the various employees who might be working the overtime. Again, Captain Cassimatis' testimony clearly showed the contrary (Ex. 47, p. 15):

"If you like me to expound on this thing, Mr. Tatum, take an example of a ship which loads scrap iron in Boston or in Portland, Maine and she is a

slow boat. She may take 45 days to go to Japan and then there is a bit of congestion and she stays 20 days outside in the anchorage. So actually the ship is getting two months' overtime for nothing. It appears that it gets the money for nothing, but on the other hand, she may go into Japan on the charter and it happens to be the Holy Week, which the crews are supposed to get three days' holidays, and the Japanese are working day and night so you've got to pay perhaps double the amount of what you should in overtime. But this is a question which works itself out with the law of averages. But as long as it takes two months from Portland, Maine to Japan there was never a case of a time charterer saying 'Because the ship was at sea and the ship is not doing anything for us more than the routine duty of sailing we won't pay overtime'. There is no such a case to my knowledge."

The trial court should be affirmed on this point and the judgment in favor of Owners against Amtro should be upheld.

CONCLUSION

It is respectfully submitted that the District Court should be affirmed. It correctly interpreted the provisions of the voyage charter to place responsibility for demurrage and unpaid freight upon Schnitzer. Having seen and heard the witnesses from Amtro, Schnitzer and Seacharter Co., Inc. the trial court found Schnitzer to be the author of the voyage charter and that Schnitzer itself interpreted the voyage charter to impose liability upon Schnitzer for the demurrage and unpaid freight.

Even under Schnitzer's theory of the case, it cannot escape payment because the incredible congestion in Japan prevented the exercise of a lien upon the cargo. The District Court properly held that once the vessel went on demurrage, laytime exclusions are of no further effect. Amtro's claim with reference to the overtime clause of the voyage charter is without merit.

Respectfully submitted,

LOFTON L. TATUM

WOOD, WOOD, TATUM, MOSSER & BROOKE
Proctors for Cia. Estrella Blanca, Ltd.

CERTIFICATE OF COUNSEL

I certify that, in connection with the preparation of this brief, I have examined Rules 18 and 19 of the United States Court of Appeals for the Ninth Circuit and that, in my opinion, the foregoing brief is in full compliance with those rules.

LOFTON L. TATUM

FEB 14 1967

No. 20526

IN THE

United States Court of Appeals

FOR THE NINTH CIRCUIT

SCHNITZER STEEL PRODUCTS CO., a corporation,
Appellant,

vs.

CIA. ESTRELLA BLANCA, LTD., as owner of the S.S.
NICTRIC, and AMTRO CORPORATION, S.A.,
Appellees.

AMTRO CORPORATION, S.A.,
Cross-Appellant,

vs.

SCHNITZER STEEL PRODUCTS CO., a corporation, and
CIA. ESTRELLA BLANCA, LTD.,
Cross-Appellees.

Brief for Appellee Amtro Corporation, S.A. An-
swering the Appeal of Schnitzer Steel Products
Co.

ALEX L. PARKS,
DUSENBERY, MARTIN, BEATTY, PARKS &
TEMPLETON,
1107 Standard Plaza,
Portland, Oregon 97204,

ROBERT A. FLETCHER,
FLETCHER & RAUCH,
4050 Wilshire Boulevard,
Suite 408,
Los Angeles, Calif. 90005,
*Proctors for Appellee, Amtro
Corporation, S.A.*

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CIA. ESTRELLA BLANCA, LTD.,
Cross-Appellees.

Brief for Appellee Amtro Corporation, S.A. Answering the Appeal of Schnitzer Steel Products Co.

In answer to Schnitzer's appeal, Amtro adopts the brief of Owners, Cia. Estrella Blanca, Ltd. We wish to add only the following:

I.

The District Court Did Not, as Schnitzer Asserts, Construe the Lien Clause (Clause 8) Out of the Voyage Charter. The Charter Placed on Schnitzer the Absolute Obligation to Pay the Demurrage and Balance of Freight and Also Gave Amtro a Lien on the Cargo as Additional Security for That Obligation.

Schnitzer's attack on the District Court's interpretation of the voyage charter is based on a mis-state-

ment of the District Court's holding. Schnitzer repeatedly accuses the District Court of reading all of printed clause 8 out of the charter, and of holding that the charter gave no lien on the cargo.¹ The District Court held nothing of the sort. What it did hold was that the unqualified promise by the charterer (Schnitzer) to pay the demurrage in typewritten clause 18 and in the typewritten substitution to clause 7 overrode and superseded the qualified obligation *in the last sentence* of printed clause 8 to pay these sums "only to such extent as the owners have been unable to obtain payment thereof by exercising the lien on the cargo." While the District Court did hold correctly that the lien on cargo could not be exercised under prevailing conditions in Japan, the court recognized that *the charter* gave the lien as an additional remedy.²

¹This mis-statement of the holding of the District Court occurs again and again in Schnitzer's brief; in the Statement of the Case (page 6):

"The Court held that Clause 18 of the voyage charter party modified and superseded Clause 8, so that the latter was ineffective and that no lien on the cargo was given for unloading demurrage and unpaid freight."

In the statement of the questions on appeal (page 12):

"1. Whether the Court misconstrued the voyage charter party in holding that Clause 8 (the lien or cesser clause) was modified out of existence by Clause 18, so that there was no lien given on the cargo for demurrage . . ."

In the specifications of error (page 13):

"1. The Court erred in entering a decree (R. 153) against Schnitzer Steel Products Co. for any sum other than \$500 stevedore damage admittedly due (R. 106), in that the Court's conclusion that Clause 8 (cesser clause) was not a part of the charter party between Amtro and Schnitzer, was an erroneous construction of the charter party . . ."

And in the Argument (page 47):

"In support of its conclusion that the lien of the cesser clause was not intended to be operative, the Court also found that . . ."

²See the following statements in the District Court opinion (the italics ours):

"Obviously, the requirement that payments of demurrage be made in United States currency would not have been inserted

What was accomplished by the various typewritten additions and deletions in the voyage charter is clear, and was correctly understood by the District Court:

1. The changes transformed what had been, under the printed Gencon form, the obligation of "*merchants*", *i.e.* the consignees of the cargo, to discharge the vessel within the lay time into an obligation *by charterers* to do so. The language is fully analyzed in Owners' brief. The change was made by crossing out printed clause 6 of the Gencon form, which had placed the discharge obligation on merchants, and substituting typewritten clauses 17 and 18 which obligated charterers to discharge, and to do so within the lay time. Whether Schnitzer passed on the discharge obligation to the consignees under its sales contracts with them has nothing to do with the voyage charter contract between Amtro and Schnitzer. Schnitzer is the party which undertook the absolute obligation toward Amtro that the vessel be discharged within the stated time.

if the parties had intended an *exclusive* remedy of foreclosure and sale under *the lien provision*." [R. Vol. I, p. 139, lines 15-19].

"The original Clause 8 was nothing more than the so-called 'cesser clause' in the classic *GENCON* charter. Where such a clause is *modified*, as here, by the agreement of the parties, the *modification* prevails over the original clause." [R. Vol. I, p. 140, lines 22-25].

"It is my conclusion on the evidence that Japan has a lien law that might be exercised in the hands of consignees within two weeks after delivery, but that such law was not applicable to the facts in the present case for the obvious reason that the scrap was delivered to persons other than the consignees and that Amtro was not in a position to *effectively assert its lien* on account of the representations of Schnitzer that the demurrage and unpaid freight would be paid. Even if Clause 8 remained in *full* force and effect, not *modified* by the typewritten language, the provision with reference to the exercise of the lien being *the sole remedy*, it should not be enforced on the record before me." [R. Vol. I, p. 144, lines 13-24].

2. The changes in the charter likewise transfer the primary and personal obligation to pay the demurrage from “merchants” to “charterer” (*i.e.* Schnitzer). This is done by crossing out the following language of printed clause 7:

“7. Ten running days on demurrage . . . payable day by day, to be allowed merchants all together at ports of loading and discharging”

and inserting in its stead and right above it the typewritten words:

“Demurrage, if incurred, to be paid by charterers.”

This is re-emphasized in typewritten clause 18 of the rider which provides, immediately following the language establishing the length of time for loading and discharge:

“. . . If longer detained, charterers to pay demurrage at the rate stipulated in clause 7 and payments to be made in the same currency as freight payment.”

3. This unqualified and primary obligation placed upon charterers to pay the demurrage in the Nictric charter obviously supersedes the qualified and secondary obligation placed upon charterers by the last sentence of printed clause 8 of the Gencon form. This is precisely what the District Court held.

4. These changes are not in conflict with, and do not eliminate, the lien on cargo for the freight and demurrage given by the first sentence of clause 8. Instead, they transform that lien from what had been, under the original Gencon form, a lien to secure payment by the consignees into a lien to secure the payment by Schnitzer of Schnitzer's obligation.

There is nothing unusual about such a lien. It is the familiar maritime lien upon the goods *in rem*, independent of *in personam* rights. Such maritime liens commonly exist on property although the personal obligation is owed not by the owner of the property, but by someone else.

“ . . . The maritime lien in our admiralty jurisprudence attaches irrespective of personal obligation on the part of the owner of the ship or cargo.”

Robinson, Admiralty (1936), p. 364;

The Barnstable, 181 U.S. 464, 467, 21 S. Ct. 684, 685, 45 L. Ed. 954 (1901).

For example, where cargo is carried on a chartered vessel under bills of lading issued only by the charterer, the charterer, and not the owner of the vessel is personally liable for the performance of the contract of carriage, but cargo also has a maritime lien upon the vessel to secure that performance.

The Albert, 61 Fed. 113 (2d Cir. 1894);

The Poznan, 276 Fed. 418, 432-3 (S.D.N.Y. 1921—L. Hand, D.J.)

Similarly, when a vessel subject to a maritime lien for an obligation of its then owner is thereafter sold, the vessel remains subject to the lien although the new owner is not personally liable, and only the former owner is.

Libbie Purdy, 32 Fed. Supp. 67, 1940 A.M.C. 416 (D. Mass. 1940);

Henry S, 4 Fed. Supp. 953, 1933 A.M.C. 1401 (E.D. Va. 1933).

The owner of the property may as a practical matter be required to satisfy or post security against the lien

claim, but he is then entitled to pursue the party who is personally liable for indemnity.

The maritime lien and the *in personam* rights are cumulative. The creditor may at his election pursue one or the other, or both at once, until he is paid.

Golden Gate, 52 Fed. 2d 397, 1931 A.M.C. 1632, 1636 (9th Cir. 1931); cert. den. 284 U.S. 682, 52 S.C. 199, 76 L. Ed. 576;

The Eastern Shore, 24 Fed. 2d 443, 1928 A.M.C. 327 (D.C.Md. 1928);

The Brothers Agap, 34 Fed. 352 (D.C.N.Y. 1888).

The party personally liable has no right to complain if the creditor pursues him exclusively, instead of pursuing the lien on the goods. Indeed, when both remedies are pursued in one action, the party personally liable is held to the primary liability, and the goods are liable only secondarily, as security in the event that collection cannot be made from the party primarily liable.

The Barnstable, cited *supra*;

The Harper No. 145, 42 Fed. 2d 161 (2d Cir. 1930), cert. den. 282 U.S. 875, 51 S.Ct. 79, 75 L. Ed. 772.

Thus the voyage charter, as correctly interpreted by the District Court, placed the *in personam* obligation on Schnitzer for the demurrage and the balance of the freight, and gave the vessel a lien on the cargo to secure payment by Schnitzer. This is the only interpretation which fits the analysis of the historical background and business purpose of lien clauses which Schnitzer itself makes in its brief (pp. 36-39). As Schnitzer's

counsel say, the purpose of the clause historically and in most charters is to allocate responsibility for the unloading demurrage so that it places incentive on those responsible for discharge to accomplish it with a minimum of delay, and to require the vessel to collect unloading demurrage and unpaid freight from the parties primarily liable for it, at a time when the pressure is greatest upon them to meet that liability. In the unmodified printed Gencon form, the parties responsible for discharge, and therefore the parties primarily liable for the demurrage, were the consignees. Under the terms of the Nictric voyage charter, Schnitzer, and not the consignees, was the party responsible to Amtro and the vessel for the discharge, and Schnitzer was the party which undertook that the discharge would be completed within the specified time. Therefore, the primary obligation to pay demurrage must be upon Schnitzer, and the lien must be to secure payment of Schnitzer's obligation.

Schnitzer might, as it now contends in its brief, have received a tactical advantage if Amtro and owners had been able to exercise the lien, since Schnitzer might have been able to beat the consignees down when they came to pursue their indemnity rights against Schnitzer. This is not a calculation which the law can respect. Schnitzer, as the party personally and primarily liable, would have had no right to complain even if Amtro and Owners had chosen to pursue Schnitzer alone, without paying any attention to the lien at all.

II.

The Foregoing Construction of the Charter Was the One Followed by Amtro While the Charter Was in Effect and Now. Only Schnitzer Changed Its Construction as Its Advantage Dictated.

Schnitzer's brief seeks to excuse what the District Court found to be Schnitzer's "indefensible" reversal of its interpretation of the charter by accusing Amtro of a similar change. To make this argument possible, Schnitzer mis-states Amtro's contentions in this litigation. Schnitzer's brief says (p. 46).

"Thus, the only change of position in this litigation is that of Amtro, which now claims that there was no lien on the cargo for demurrage and that Clause 8 of the charter party was not in effect."

Schnitzer cites nothing in the record to support this assertion. It is untrue.³ The interpretation of the charter urged by Amtro before the trial court and before this

³Amtro's pleadings [Answer, R. Vol. I, pp. 8-13 and Cross-Libel, R. Vol. I, pp. 15-24] are bare of any such claim. The statement of Amtro's contentions on the subject in the pre-trial order [R. Vol. I, p. 109] was:

"3. The typewritten addendum to the voyage charter, coupled with typewritten amendments to the body of the printed voyage charter, prevail over the printed language of clause 8 of the voyage charter, and by reason thereof Amtro had no obligation, as stated in said clause 8, to endeavor first to obtain payment of freight and demurrage by exercising a lien on the cargo."

The statement is that by reason of the typewritten changes Amtro had no obligation to endeavor first to obtain payment by exercising the lien, which is what Amtro still contends, not that Amtro had no lien. Amtro's position was extensively covered in briefs filed with the trial court, and it is hard to see how Schnitzer's counsel could misunderstand at this stage of the proceedings.

Court is the one set out in the foregoing section of this brief.

This was also the interpretation maintained by Amtro at all times while the charter was in effect. This is why Amtro did not make demand upon the consignees for payment of the demurrage.⁴ This is why all the demands for payment of the demurrage, from the time the demurrage commenced to accrue, were made upon Schnitzer. It was upon this interpretation of the charter that Amtro's counsel, after Schnitzer had ignored demands for the demurrage for about a month, directed to Schnitzer the telegram [Ex. 101, R. Vol. II, p. 103] announcing Amtro's intention to exercise the lien unless *Schnitzer* guaranteed and adequately secured payment of the demurrage. This is why, on December 7, 1961, when Schnitzer repudiated what Amtro understood to be Schnitzer's firm agreement to pay the undisputed portions of the demurrage immediately and to arbitrate the disputed amounts [see the Finding of the District Court, R. Vol. I, p. 141, lines 10-12], Amtro attempted to go ahead with the exercise of the lien until it was advised that under the conditions prevailing in Japan the lien could not be exercised.

⁴The only demand ever made upon the consignees by Amtro is the one contained in Exhibits 106, 107 and 107A, letters written to the consignees by Amtro's counsel on December 21, 1962, nearly a year later. These were written long after the present litigation was instituted, and long after Schnitzer's counsel had begun to press Schnitzer's present theory that the consignees were liable for the demurrage. As stated in Mr. Fletcher's uncontradicted testimony [R. Vol. II, p. 124, lines 8-13], these notices were sent in order to extend the Japanese statute of limitations for another year. No lawyer likes to let time run on any claim even under his opponent's theory of the case, and even though he disagrees with that theory, if a simple notice will stop it. Suing on what one believes to be an unfounded claim is quite another thing, and Amtro finally allowed the statute to run with respect to any claim against the consignees.

This interpretation of the charter is also the one acted upon by owners and their agents in Japan. The communication which Dodwell & Co. Ltd. addressed to the consignees on November 27, 1961 [Ex. F-1 to deposition of Saishoji, trial Ex. 44E] was not a demand for the demurrage against the consignees *in personam*, but merely a notice that the owners intended to exercise the lien if the demurrage was not paid. The object was to advise the consignees that if they wanted their cargo, they should take "the necessary action", *i.e.* get Schnitzer to pay its demurrage obligation. This is further confirmed by the following at the conclusion of Dodwell's cable to owners of December 9, 1961 [Dep. Ex. F4 to trial Ex. 44E, 20-22, 44G 171-172, quoted nearly in full on pages 56 and 57 of Schnitzer's brief]:

"RECOMMEND YOU CONTINUE EFFORTS
GUARANTEE FROM VOYAGE CHARTER-
ERS MEANWHILE WE WILL EMPHASIZE
TO RECEIVERS INTENDED LIEN *AND*
POSSIBLY THEY WILL PRESSURIZE
SCHNITZER GIVE SECURITY"

It was Schnitzer which insisted, until after the cargo had been discharged and delivered and any lien had been lost, that there was no lien on the cargo, and now turns around and contests liability on the basis of Amtro's failure to exercise that very same lien. The evidence supporting the District Court's findings of fact to that effect is quoted and discussed on pages 13-19, 35-37 of Owners' brief.

Amtro's counsel were seriously worried about the possible merit of Schnitzer's contention that Amtro had no lien on the cargo. It was indisputable that if, as Schnitzer was contending, the demurrage, like the bal-

ance of the freight, was not due until after completion of the discharge, the lien was invalid, since the maritime lien on cargo for demurrage and freight is dependent upon possession and lost by delivery of the cargo (see the authorities cited on p. 27 of Owners' Brief). Amtro's view was that under the charter the demurrage became due as incurred. But Amtro's counsel was forced to realize that the charter was most ambiguous on the point, since, as Schnitzer kept pointing out, the language requiring payment of demurrage "day by day" in printed clause 7 had been crossed out. Schnitzer's contentions added greatly to the hazards of any exercise of the lien, but since the lien was the only practical weapon Amtro had with which to compel immediate payment, Amtro had to try to pursue it.

Schnitzer attempts to argue (brief, pp. 74-75) that Amtro knew of Schnitzer's change of position on December 7, 1961, and that this was in time for Amtro to have gone ahead and exercised the lien undeterred by what Schnitzer had said previously. The District Court found to the contrary. It found [R. Vol. I, p. 141, lines 7-9]:

"Schnitzer relied on this construction of the contract from about November 17 until after the cargo had been discharged on December 31."

The words "this construction" refer to that stated immediately previously in the opinion, namely that Schnitzer agreed to pay the demurrage, but that the demurrage and balance of the freight were not payable until completion of discharge, and that there was no lien on the cargo for the demurrage. The above-quoted finding is fully supported by the evidence. It is true that on December 7, 1961, Mr. Krause informed Mr. Fletcher

that Schnitzer was not going to go through with the agreement which Mr. Krause had previously said that his clients had authorized him to accept [R. Vol. II, pp. 109, 113]. However that agreement had called for the immediate payment of the demurrage incurred to date, not postponement of the entire payment until completion of discharge [Par. 3, Agreement annexed to Amtro's Ex. 68]. On the matter of the lien, Mr. Krause said only that:

“[Amtro] had better take whatever remedies [Amtro] thought [it] had [R. Vol. II, p. 113, line 20, to p. 114, line 1].

There is testimony by Mr. Lewis, one of Schnitzer's counsel, that on December 11, after he had been unable to beat down the amount which Schnitzer was to pay, he told Amtro's counsel “lien the cargo” [R. Vol. II p. 224, line 14]. Mr. Fletcher's testimony on what was said at that meeting is not in accord with Mr. Lewis [R. Vol. II, p. 114, line 22, through p. 115, line 14]. Even if Mr. Lewis' version is accepted (and the District Court was not required to accept it), his statement did not amount to a retraction of Schnitzer's previous position toward Amtro that any lien on the cargo which Amtro might seek to exercise was invalid under the terms of the charter. The purport of his statement in the context was merely “try it if you think you can.” This is shown beyond doubt by the letter written by Mr. Krause on behalf of Schnitzer to Owners, and dated December 6 and received by Owners' counsel December 8 [Lib. Ex. 34], which specifically reiterates Schnitzer's position that there was no lien, that owners would be held liable for damages if they attempted to exercise a lien, and that nothing was due prior to discharge of the vessel.

When on December 12, 1961, Mr. Fletcher advised Mr. Lewis that Amtro had learned that it was impossible to exercise the lien, Mr. Lewis' only response was, "Oh, that's interesting" [R. Vol. II p. 115, line 23, through p. 116, line 6]. Mr. Lewis' testimony does not contradict this [R. Vol. II p. 225, line 2]. Thereafter, there was only silence from Schnitzer. Owners' libel on December 14 specifically advising Schnitzer that it was impossible to obtain payment of the demurrage by exercising a lien on the cargo was met with further silence. On December 26, 1961, while a little cargo still remained on board, Amtro's counsel telegraphed Schnitzer demanding payment of demurrage and freight upon completion of discharge, when Schnitzer had contended that it was payable, and placing Schnitzer on notice that failure to pay would cause Amtro the loss of its time charter with owners [Amtro Ex. 60]. Schnitzer left this telegram unanswered until 9:47 P.M. Pacific Standard time on December 29, 1961. This was $2\frac{1}{4}$ hours before the completion of the Nictric discharge in Japan (under the Admitted Facts, when the International Date Line is taken into account, see footnote 3, p. 13, Amtro's Op. Br., for the citations to the record). At that time Schnitzer sent to Amtro a telegram [Amtro Ex. 61] reading:

"YOUR TELEGRAM RE NICTRIC DATED 12/26/61 RECEIVED WE HAVE NOT ASSUMED NOR AGREED TO PAY DEMURRAGE UPON COMPLETION OF DISCHARGE. WE DENY ALL LIABILITY FOR DEMURRAGE AND BALANCE OF FREIGHT."

That telegram was no more than an unexplained denial of liability. It contained no hint that Schnitzer had reversed its prior position on the invalidity of Amtro's lien under the charter, or that it denied liability *because* Amtro should have exercised the lien. No notice whatever of the position Schnitzer finally took in the trial court, or is taking upon this appeal, was ever communicated to Amtro or owners until months later.

On that record, Schnitzer's actions can be explained only in one of two ways: Either

(1) When Schnitzer received notice on December 26, 1961, that failure to pay upon the completion of discharge would break Amtro, Schnitzer interpreted the charter in the same way as it always had previously, and knew that it was liable, but wanted to break Amtro in the hope that if Amtro were defunct, Schnitzer could settle its obligation cheaply with Owners, who could be made whole with only part of the demurrage; or

(2) When Schnitzer learned on December 11 that Amtro believed that the lien could not be exercised, it then decided that if it switched its charter interpretation, and kept quiet about the switch until after all the cargo had been discharged and delivered, it might be able to dig up some evidence later to suggest that a lien might have been exercised, and escape liability entirely.

On either explanation Schnitzer's conduct is "indefensible," as the District Court found. On either explanation, the District Court correctly held Schnitzer liable for the full freight and demurrage. The District Court should also have awarded to Amtro, under the legal principles set out in Amtro's Opening Brief on the Cross-Appeal, recovery for the damages caused to it by Schnitzer.

Conclusion.

It is accordingly respectfully submitted that the District Court should be affirmed on the issue of Schnitzer's liability for freight and demurrage, and should be directed to grant to Amtro against Schnitzer the further relief sought by Amtro's Cross-Appeal.

Respectfully submitted,

ALEX L. PARKS,
DUSENBERY, MARTIN, BEATTY,
PARKS & TEMPLETON,

ROBERT A. FLETCHER,
FLETCHER & RAUCH,

*Proctors for Appellee Amtro
Corporation, S.A.*

Certificate.

I certify that, in connection with the preparation of this brief, I have examined Rules 18 and 19 of the United States Court of Appeals for the Ninth Circuit, and that, in my opinion, the foregoing brief is in full compliance with those rules.

ROBERT A. FLETCHER

FEB 14 1967

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REPLY BRIEF OF APPELLANT
SCHNITZER STEEL PRODUCTS CO.

Upon Appeal from the United States District Court
for the District of Oregon

HONORABLE JOHN F. KILKENNY, Judge

GUNTHER F. KRAUSE,
CARL R. NEIL,
KRAUSE, LINDSAY & NAHSTOLL,
Ninth Floor, Loyalty Building
Portland, Oregon 97204,
Proctors for Appellant,
Schnitzer Steel Products Co.

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as Owner of the SS NICTRIC,

Cross-Appellees.

REPLY BRIEF OF APPELLANT
SCHNITZER STEEL PRODUCTS CO.

I

The conditional liability of Schnitzer under Clause 8 of the voyage charter party for unloading demurrage and unpaid freight was not changed to primary liability by other clauses of the charter party.

Schnitzer has set forth in its opening brief, pp. 34-50, its position that Clause 8 of the voyage charter party

(Ex. 2) allocates liability for demurrage incurred at the discharge port and for unpaid freight, and that Schnitzer as voyage charterer was liable under Clause 8 for those items only "to such extent as the Owners have been unable to obtain payment thereof by exercising the lien on cargo." Appellees in their answering briefs raise a number of arguments in support of the trial court's view that Clauses 7 and 18 of the charter party make Schnitzer as voyage charterer primarily liable for these sums by impliedly eliminating the condition on Schnitzer's liability set forth in Clause 8. Most of these arguments are answered by Schnitzer's opening brief, and we shall reply to only a few of them here.

Appellees argue that the term "merchants" as used in the original printed charter party form meant cargo receivers, and that deletion of that term in Clause 7 suggests that charterers were to become primarily liable for demurrage at the discharge port. It is true that Clause 8 of the charter party contemplates that cargo receivers will be primarily responsible for demurrage incurred at the discharge port, and that the charterer is only secondarily liable to the extent that the lien on cargo given by Clause 8 cannot be exercised. Clause 8, however, does not refer to "merchants" in allocating this liability. Liability is imposed on cargo receivers by the charter party giving the vessel a lien on cargo, in contemplation that the charterer will bind the cargo receivers to this liability by issuance of bills of lading incorporating the charter party, including the cesser clause. When receivers accept delivery of cargo under bills of lading so phrased, they agree to their responsibility for unloading demurrage and

unpaid freight as imposed upon them by Clause 8. See *Yone Suzuki v. Central Argentine Railway*, 27 F.2d 795, 800, 805 (CCA 2 1928), cert. den. 278 U.S. 652; *The Lake Galera*, 60 F.2d 870, 879 (CCA 2, 1932), and other authorities discussed at pp. 37-38 and 48-49 of Schnitzer's opening brief.

The deletion of the term "merchants" from the original printed language of Clauses 6 and 7 of the charter party does not suggest any intention to change the liability allocation of Clause 8. "Merchants" as used in the original printed form is a general term, encompassing both shippers and receivers of the cargo. Original Clause 6 referred to merchants receiving and discharging the cargo. Original Clause 7, however, allowed "merchants" ten running days on demurrage *at ports of loading and discharge*. Since Clause 8 and original Clause 5 placed responsibility for loading and demurrage at the *loading* port on charterers, "merchants" in original Clause 7 obviously referred both to charterer-shippers and receivers of the cargo. When the charter party wished to refer specifically to cargo receivers or to shippers, as opposed to both, it used those precise terms. See, e.g., references to "receivers" in original Clause 4, Clause 42 and the Strike Clause, and references to "shippers" in Clause 5 and the War Clause.

Clause 18 modified the laydays and calculation of demurrage which was specified in the original printed language of Clauses 5, 6 and 7. These clauses in the original charter party called for a specified number of laydays for loading, a specified number for discharge,

and ten days on demurrage at a specified rate, and said nothing about demurrage in the event that delay exceeded those ten days. By deleting portions of these clauses, and adding Clause 18, the parties created a different method of calculating laydays: a total of 23 weather working laydays were given both for loading and discharge, and a rate was agreed upon for demurrage after the laydays expired. In this scheme, deletion of original Clause 6 and a part of original Clause 7, including the term "merchants," was necessary. Thus, the elimination of references to "merchants" in the original printed language of those clauses had nothing whatever to do with changing the allocation of liability for demurrage specified in Clause 8.

If the parties had intended to remove the condition on Schnitzer's liability for unloading demurrage set forth in Clause 8, they would have deleted the final clause of Clause 8, leaving the last sentence reading:

"Charterers shall also remain responsible for freight, and demurrage incurred at port of discharge. [but only to such extent as the Owners have been unable to obtain payment thereof by exercising the lien on the cargo.]"

There are deletions from the original language of Clause 8 in three places, but the condition on Schnitzer's liability for unloading demurrage, bracketed in the above quotation, is not deleted. The plain inference is that all of original Clause 8 not deleted including the condition on Schnitzer's liability, was intended to remain effective.

Contrary to Owners' brief (page 9), *The Luossa*, 1936 AMC 213 (Arb. 1935), involved a claim that an added Clause 18 modified Clause 8 of the original printed Gencon form. Clause 8 in that case was identical to Clause 8 here. The vessel owners argued in *The Luossa* that Clause 18 of that charter party modified the demurrage liability allocation of Clause 8, and thus eliminated the requirement that owners show inability to exercise the lien as a condition of recovering demurrage incurred at the discharge port. Clause 18 in *The Luossa* charter party provided:

"18. In case of demurrage or other claims, owners agree to a Bank guarantee on a first-class bank, until the claim is definitely settled later on between owners and charterers by arbitration in New York."

The arbitrators held that Clause 8, not having been stricken out of the charter party, was to be given effect, and that the reference to possible demurrage liability of the charterer in Clause 18 referred to the limited demurrage liability set forth in Clause 8 of the Gencon form:

"In an effort to avoid dismissal of owner's claims upon technical grounds, we have also given full consideration to the relation of Clauses 8 and 18. While it might have been the function of the typewritten clause (18) to supersede the printed clause (8) we have concluded that unless the parties had intended both to be given effect, they would have stricken out Clause 8. As the clauses stand, obviously they both must be given effect if it is possible to do so. In the absence of any proof to the contrary, we are, therefore, forced to the result that Clause 18, insofar as it concerns demurrage, can only refer to demurrage

at loading port or to such demurrage at discharging port as owner is unable to collect by the enforcement of its lien." (1936 AMC at 216-217)

The Luossa is also in point as rebuttal to Appellees' contention here that the requirement of payment of demurrage in United States currency indicates some intention that Schnitzer, as opposed to the Japanese consignees, was to be primarily liable for unloading demurrage. The charter party in *The Luossa* required payment of unloading demurrage in U. S. currency, but it was not even suggested there that this had any bearing on demurrage liability, which it plainly does not. Japanese firms engage in substantial trade with the United States, and receive payment for exports to the United States in our currency, which makes U. S. dollars available in Japan or in this country for payment of Japanese obligations requiring that currency. International banking departments, including those in Japan, are geared to make arrangements on behalf of their customers for paying and receiving in currencies of many countries amounts owed to or by Japanese importers and exporters.

Nor is the fact that the balance of freight was payable upon completion of discharge inconsistent with the condition of Clause 8 on Schnitzer's liability. If Amtro felt that the small amount of remaining freight might not be paid on completion of discharge, it could simply have demanded security for payment and have refused to complete discharge until security was given by the consignees or the funds put in escrow pending completion of delivery.

In support of their contention that Schnitzer was the author of the voyage charter party and chargeable with an ambiguity in its terminology, appellees urge that Seacharter Company, the charter broker, acted as agent for Schnitzer in its discussions with Amtro and its agents as to the terms of the charter party. As evidence, they point to testimony of Kimberk that Captain Jensen of Seacharter Company told him that Seacharter was an agent of Schnitzer. Kimberk, however, also testified that he had never confirmed this with Schnitzer, the alleged principal, and that he had never seen a written authorization for the alleged agency (Ex. 79, p. 9). It is familiar law that an alleged agent's statement that he is an agent is not sufficient to prove his agency for the alleged principal. RESTATEMENT OF AGENCY 2D Section 285.

It is immaterial, in any event, whether or not Seacharter acted as agent of Schnitzer, rather than as an independent charter broker. The role of Schnitzer and its alleged agent in drafting the charter party was simply to submit as a sample for discussion the charter party of the KEHREA, after which the parties agreed upon appropriate modifications for the NICTRIC and the particular voyage contemplated. See discussion of the evidence in Schnitzer's opening brief, p. 42. There was no evidence as to who had drawn the similar provisions on demurrage in the KEHREA charter party, nor of any discussion between the parties to the NICTRIC charter party as to the allocation of liability for demurrage. Mr. Bettinger of Seacharter Company testified as follows (Tr. 155-160):

"Q. Are you familiar with the Gencon form of charter party?

A. Yes.

Q. Was anything said during the negotiations of the NICTRIC concerning a cesser clause? Did Amtro ever tell you that they wanted the cesser clause eliminated from this charter party?

A. No.

Q. When the charter was fixed, was your understanding that the cesser clause was a part of this charter party?

A. Yes sir.

Q. Nobody ever said anything to the contrary to you?

MR. PARKS: Your Honor, the charter speaks for itself. It has got a cesser clause in it.

THE COURT: Of course, wherever it speaks for itself that is going to control.

BY MR. LEWIS:

Q. Did any party ask you to eliminate the provisions of the cesser clause.

A. No.

Q. Did Amtro ever raise this question at all about the cesser clause, that they didn't like it?

A. No.

Q. Have you negotiated charters where the cesser clause was eliminated?

A. I have never negotiated such charters, no."

As Mr. Bettinger's testimony indicated, the cesser clause is a common part of the charter party on scrap shipments. To the same effect is the testimony of Mr. Leonard Schnitzer that in 200 charter parties involving Schnitzer, the cesser clause had been in all of them, except in one case where the parties specifically agreed

that it should be deleted (Tr. 198). In view of the lack of discussion among the parties as to any modification of the usual cesser clause or of its allocation of liability for demurrage and unpaid freight, it may be inferred that the usual operation and effect of the clause was intended, in the absence of any evidence to the contrary.

Concerning the "uncontradicted" testimony of Mr. Fletcher (Tr. 107) that Mr. Krause, Schnitzer's counsel, on November 17, 1961, asserted that Amtro had no lien on the cargo, we invite the Court's attention to Dep. Ex. F19, a report letter dated November 27, 1961, from Amtro's Mr. Stewart to its agent, Mr. Morgan. In this letter, Mr. Stewart wrote:

"Re: NICTRIC demurrage.

I have had one hell of a time with the Schnitzer crowd regarding the demurrage. As of this date they have not paid anything towards the demurrage charges. I asked our attorney to help resolve this situation. He has placed them on notice, that if the demurrage charges were not paid up to date, we would exercise a lien on the cargo. *Schnitzer has taken the position, that for us to go ahead and lien the cargo.*" (Emphasis supplied)

This is hardly consistent with Mr. Fletcher's testimony. Mr. Krause could not have taken the witness stand to contradict Mr. Fletcher without depriving Schnitzer of counsel for the balance of the trial. Schnitzer's other attorney at the trial, Mr. Lewis, was called as a witness (Tr. 220). Schnitzer's counsel had no reason to anticipate that Mr. Fletcher would take the stand and testify as to statements allegedly made by Mr. Krause. Mr.

Fletcher's taking the stand did not deprive Amtro of counsel, since Mr. Parks was on hand as Amtro's associate counsel and took over examination of witnesses after Mr. Fletcher testified (Tr. 132).

Much is made in Amtro's answering brief of Schnitzer's alleged "misreading" of the Court's opinion as to the construction of the charter party. The Court did not hold, Amtro says, that Clause 18 modified Clause 8 to the extent of eliminating the lien on cargo for unloading demurrage and unpaid freight; Clause 8 was modified only to the extent of eliminating the condition on Schnitzer's liability of the vessel's inability to exercise the lien on cargo. The Court's opinion can be read as holding that Clause 8, including the lien on cargo, was superseded by Clause 18.¹ If, however, the opinion is read as holding only that the condition on Schnitzer's liability set forth in Clause 8 (inability to exercise the lien on cargo) was eliminated by Clause 18, our point is the same: all parties assumed until after this case was filed and after cargo discharge was completed that Clause 8 was fully in effect and that inability of Amtro

¹ See R. 144, lines 21-24:

"Even if Clause 8 remained in full force and effect, not modified by the typewritten language, the provision with reference to the exercise of the lien being the sole remedy, it should not be enforced on the record before me." (Emphasis supplied)

And see R. 141, lines 5-9 and 20-22:

"Subsequently, Schnitzer's counsel took the position that in fact there was no lien on the cargo for the demurrage. Schnitzer relied on this construction of the contract from about November 17th until after the cargo had been discharged on December 31st. . . . Until December 7th, it is quite clear that Schnitzer interpreted the contract in line with Amtro's and this Court's conclusions." (emphasis supplied)

to exercise the lien was a condition to Schnitzer's liability for demurrage incurred at the discharge port. See pleadings and evidence cited at pp. 43-46 of Schnitzer's opening brief. See also Dep. Ex. B-2, a cable from owners to Dodwell on December 28, 1961, advising the latter of the filing of this suit and instructing them nevertheless to "endeavour exercise lien view keeping voyage charterers responsible under Clause 8 voyage charter."

Thus, there is no reason to believe that the parties to the voyage charter intended to modify the usual operation of the cesser clause as set forth in Clause 8 of the charter party. Its operation was to impose upon the consignees liability for demurrage incurred at the port of discharge and for unpaid freight, when cargo was accepted by them under bills of lading incorporating the terms of the voyage charter party. See discussion and cases cited at pp. 36-38, 48-49 of Schnitzer's opening brief. Schnitzer as voyage charterer remained liable to Amtro for these amounts, as Clause 8 provides, only to the extent that Amtro was unable to collect the demurrage and unpaid freight from the consignees by exercise of its lien on the cargo.

II

Appellees failed to prove that Amtro was unable to collect the demurrage and unpaid freight from the consignees by exercise of the lien on cargo, and thus failed to meet the condition stated in Clause 8 of the charter party on Schnitzer's liability.

Here again, Schnitzer's opening brief, pp. 51 et seq., rebuts most of the points argued in Owners' answering

brief (pp. 24-37), and we shall confine our reply to comment on a few of the answering arguments.

Owner's brief, like the District Court's opinion, attempts to shift to Schnitzer the burden of establishing that the lien on cargo could have been exercised. The burden, however, is upon appellees under Clause 8 of the voyage charter party to prove the condition upon Schnitzer's liability, that Amtro was unable to exercise the lien. *The Luossa*, 1936 AMC 213 (1935); *The Arizona*, 63 F.2d 42, 43 (CCA 4, 1933); Tiberg, *THE CLAIM FOR DEMURRAGE* (1962), p. 55. Schnitzer has cited in its opening brief (pp. 53-68) the inadequate and *pro forma* efforts to exercise the lien, and the absence of anything other than hearsay, speculation and conclusion lacking factual support for findings that Amtro was unable to do so.

Owners claim (Br. p. 27) that the lien could only be exercised by the vessel retaining possession of the cargo either on board the NICTRIC or in lighters or ashore. That is neither the Japanese nor the American law. As the court found (R. 144), Japanese law gives a lien for demurrage on the cargo after delivery to the consignees if asserted by judicial proceedings within two weeks after delivery (Ex. 44J, pp. 231 et seq.; Dep. Ex. L-4; Ex. 44I, pp. 193, 224). Mr. Main of Dodwell & Co. testified that he had exercised liens on cargo after discharge in Japan (Ex. 44G, p. 173). American law is similar. The vessel may exercise its lien for unpaid freight and demurrage by a suit in rem against the cargo after delivery to the receivers, if delivery was made with notice

to the receivers of the vessel's claims against the cargo. *Bags of Linseed*, 1 Black 108, 17 L. Ed. 35 (1861).

Owners assert (Br. pp. 32-35) that the evidence showed delivery of the cargo directly to third parties other than the consignees, so that exercise of the Japanese lien after discharge was impossible. Owners first cite generally the testimony of Yoshida, Kayashima and Hayashibara, representatives of three of the consignees, without reference to any particular pages of their depositions. Neither Yoshida nor Kayashima was able to say when the two consignees they represented sold or delivered their cargo to third parties, or even whether it was before or after discharge from the vessel (Ex. 44B, pp. 6-7; Ex. 44C, pp. 11-12). Moreover, the District Court sustained motions to strike their testimony as hearsay (R. 124, 184-185). Hayashibara was far from certain as to when the cargo of his consignee was delivered to a third party, and failed to produce any sale or delivery documents (Ex. 44D, pp. 27-32).

The main reliance of Owners' brief, like that of the District Court (R. 142-143, 144), is on the cargo discharge survey reports (Exs. 22-27, 29). These reports show on their face that their purpose was to determine the amount and condition of the cargo. They do not purport to be records of delivery or sale by the consignees to third parties. Schnitzer objected to their admission into evidence on this ground (Tr. 10-12). The reports do not state that delivery of the cargo was to the named consumers or that the consumers, rather than the consignees, were in possession of the cargo. In some instances, the inspection evidenced by the report occurred several days

after the cargo had been discharged, with no information as to when, if ever, possession passed from consignee to consumer (e.g., Ex. 24A, showing inspection on January 6 and 9, 1962, a week after discharge of the NICTRIC was completed on December 31, 1961). It was error to admit these reports to show transfer of possession of the cargo to third parties (Tr. 10-12), and more harmful error to rely on them as establishing such transfer (R. 142-143, 144). Appellees failed to produce the negotiated bills of lading or any evidence to show whether the consignees or third parties presented the bills of lading to the master of the NICTRIC in order to receive the cargo. The vessel's master in his deposition (Ex. 47) offered no enlightenment as to the identity of the parties whom he permitted to discharge and receive the cargo from the vessel.

Owners refer to Schnitzer's objections to hearsay, speculation and conclusion without factual support, and to the District Court's reliance on it, as "technical niceties." This is not a case in which only a few incidental and harmless items of inadmissible evidence were received by the court. Nor is it a case where prejudicial matter has been erroneously admitted in evidence, but disregarded by the court in reaching its decision. The record in this case is filled with an incredible amount of hearsay, surmise, speculation and unfounded conclusion, as a reading of the testimony quoted in the Specifications of Error (Schnitzer's opening brief, pp. 14-33) or of any of the depositions admitted in evidence will show. Another example is Captain Cassimatis' testimony quoted at p. 25 of owners' brief. Moreover, the District

Court necessarily relied on much of this evidence in its findings, as is shown in Schnitzer's opening brief, pp. 61-69. The Court's findings of inability to exercise the lien rest heavily on the deposition of Dodwell's employees, Main and Saishoji. Yet both admitted that their testimony was mainly hearsay and not based on personal knowledge. See evidence cited and quoted in Schnitzer's opening brief, pp. 61-62.

Schnitzer has attempted on this appeal to restrict its specifications of error challenging the evidence and findings to those matters of inadmissible and insufficient evidence on which the Court's opinion indicates reliance. Compare the vast amount of hearsay, speculation and conclusions cited in Schnitzer's objections in the District Court to the deposition evidence (R. 123-128) with Specifications of Error Nos. 12 through 17 set forth at pp. 15-32 of Schnitzer's opening brief. To object to findings and a decree based throughout on inadmissible and unreliable hearsay and speculation is not to indulge in "technical niceties," but to assert fundamental unfairness in the trial and in the decision-making process.

As Benedict on Admiralty (6th ed. 1940) Section 381(b) points out in a passage immediately following the language quoted at p. 28 of Owners' brief, the rationale of relaxing admissibility rules in trials to a court without a jury is that the court will appreciate the absence of probative value in hearsay, speculation and the like, and will treat it accordingly in reaching its decision:

"The experienced judge may be relied upon to

appreciate the probative value of any material offered in evidence; and if he should err, the appellate court may correct the error, as an admiralty appeal is a trial *de novo*.

“The freedom in admitting evidence is largely due to the fact that admiralty cases are tried by judges, and not by juries.”

While the rules of initial admissibility may be relaxed on this rationale, neither Benedict nor the cases cited in Owners’ brief, page 28, hold that the District Court sitting in admiralty may not only receive but also base findings solely on inadmissible hearsay, speculation and surmise in the testimony of witnesses.

Owners claim (Br. pp. 28-29) that Main and Saishoji of Dodwell & Co. testified that exercise of the lien was impossible. The citations given to their deposition testimony do not support the assertion, and Schnitzer’s opening brief, pp. 54, 60-62, shows that their testimony was hearsay and conclusion lacking personal knowledge. With even less foundation in the record, Owners also assert (Br. pp. 29, 37) that their legal counsel in Japan had given contemporaneous advice that exercise of the lien on cargo in Japan was impossible. Owners cite the hearsay testimony of the NICTRIC’s master (Ex. 47, pp. 51, 59-60), which is quoted and attacked in Schnitzer’s Specification of Error No. 17. Cassimatis’ statements of what he was told are contradicted by Main’s testimony that Owners’ Japanese counsel (the McIvor firm) never advised Dodwell that exercise of the lien was impossible, legally or otherwise (Ex. 44G, p. 177-2). The letter of McIvor to Dodwell of December 13, 1961 (Dep. Ex.

B-18), shows that the facts bearing on the legal right to lien the cargo were not made available to the law firm, and that McIvor suggested only that it might be easier to sue Schnitzer than to proceed with exercise of the lien. Owners failed to call any member of the McIvor firm to testify directly as to what advice on lien exercise, if any, was given by them.

As part of their effort to shift to Schnitzer the burden of proof on the condition of inability to exercise the lien, Owners belabor Schnitzer for failing to arrange for discharge of the cargo and exercise of the lien, and imply that PacMarine as agent for Schnitzer had the power to direct and arrange for these matters. In fact, the right to control discharge and to arrange for it was solely in the consignees of the cargo, and was not within the control of Schnitzer. See sale contracts discussed in Schnitzer's opening brief, pp. 47-48, and testimony of Leonard Schnitzer, Tr. 189. Moreover, in view of the clear desire of appellees to bring suit against Schnitzer and to attempt exercise of the lien only to the extent of gathering "proof" that exercise was impossible, any suggestion by Schnitzer's agents would have been ignored by appellees.

Finally, Owners' claims that appellees were deterred from exercise of the lien by statements of Schnitzer that it would pay the demurrage are without foundation. Mr. Fletcher testified that he was told by Mr. Krause on December 7, 1961, that Schnitzer would not pay the demurrage and that he immediately thereafter instructed exercise of the lien:

"THE WITNESS: I heard nothing further from Mr. Krause following the 5th until the 7th, on

which day I called Mr. Krause and asked him where the agreement and money were. Mr. Krause told me that his clients were not—that he was informed that his clients were not going to go through with the agreement; that we had better take whatever remedies we thought we had.

Q. Did you communicate this fact to owners?

A. I communicated this fact to owners, telling them to go ahead; that that was the situation, and that they had better now go ahead and start the exercise of the lien." (Tr. 113-114)

We have demonstrated in our opening brief (pp. 60, 74-75) that Amtro and Owners in November, 1961, had commenced preparations to exercise the lien, notwithstanding settlement negotiations with Schnitzer, and that more than enough cargo remained on board the NICTRIC to exercise the lien after December 7 and until shortly before discharge was completed on December 31. Appellees chose, instead, to proceed by filing this suit against Schnitzer on December 14, and to make thereafter only token efforts to exercise the lien, with a view toward keeping Schnitzer "responsible" under Clause 8 of the charter party (see Dep. Ex. B-2).

In summary, appellees failed in their burden of showing inability to exercise the lien. The Court's findings to the contrary rest on hearsay, speculation and unfounded conclusion having no probative value. Accordingly, the condition upon Schnitzer's secondary liability under Clause 8 of the voyage charter party for unloading demurrage and unpaid freight was not met. The District Court's decision deprived Schnitzer of the benefits of

the cesser clause, by permitting appellees to ignore their obligation to collect these amounts from the consignees as the parties primarily liable. Schnitzer is without the benefits of possession or lien rights on the cargo to compel payment by the consignees.

CONCLUSION

The decree of the District Court should be set aside to the extent that it awards demurrage and unpaid freight against Schnitzer Steel Products Co.

Respectfully submitted,

GUNTHER F. KRAUSE

CARL R. NEIL

KRAUSE, LINDSAY & NAHSTOLL

Proctors for Schnitzer Steel Products Co.

CERTIFICATE OF COUNSEL

I certify that, in connection with the preparation of this brief, I have examined Rules 18 and 19 of the United States Court of Appeals for the Ninth Circuit, and that in my opinion, the foregoing brief is in full compliance with those rules.

CARL R. NEIL

Of proctors for Schnitzer
Steel Products Co.

FEB 14 1967

No. 20526.

IN THE

United States Court of Appeals

FOR THE NINTH CIRCUIT

SCHNITZER STEEL PRODUCTS CO., a corporation,
Appellant,

vs.

CIA. ESTRELLA BLANCA, LTD., as owner of the S.S.
NICTRIC, and AMTRO CORPORATION, S.A.,
Appellees.

AMTRO CORPORATION, S.A.,

Cross-Appellant,

vs.

SCHNITZER STEEL PRODUCTS CO., a corporation, and
CIA. ESTRELLA BLANCA, LTD.,
Cross-Appellees.

Opening Brief for Cross-Appellant Amtro
Corporation, S.A. on Cross-Appeal.

ALEX L. PARKS,
DUSENBERY, MARTIN, BEATTY, PARKS &
TEMPLETON,

1107 Standard Plaza,
Portland, Oregon 97204,

ROBERT A. FLETCHER,
FLETCHER & RAUCH,

4050 Wilshire Boulevard,
Suite 408,
Los Angeles, Calif. 90005,

*Proctors for Cross-Appellant,
Amtro Corporation, S.A.*

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WM. B. LUCK, CLERK

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SCHNITZER STEEL PRODUCTS CO., a corporation,
Appellant,

vs.

CIA. ESTRELLA BLANCA, LTD., as owner of the S.S.
NICTRIC, and AMTRO CORPORATION, S.A.,
Appellees.

AMTRO CORPORATION, S.A.,
Cross-Appellant,

vs.

SCHNITZER STEEL PRODUCTS CO., a corporation, and
CIA. ESTRELLA BLANCA, LTD.,
Cross-Appellees.

Opening Brief for Cross-Appellant Amtro Corporation, S.A. on Cross-Appeal.

Jurisdictional Statement.

This Cross-Appeal is from a final decree in admiralty of the United States District Court for the District of Oregon, Honorable John F. Kilkenny, Judge Presiding [R. Vol. I, pp. 152-154; 130-149]. That decree is in an action by Cia. Estrella Blanca, owner of the vessel S.S. NICTRIC (hereinafter referred to as "Owners" in this brief) against the time-charterer of the vessel, Amtro Corporation, S.A. (hereinafter referred to as "Amtro" in this brief) commenced by libel and foreign attachment garnishing all amounts owing by

Schnitzer Steel Products Co. (hereinafter referred to as "Schnitzer" in this brief) to Amtro under a voyage charter of the vessel by Amtro to Schnitzer, in which Amtro appeared, filed claim, and asserted its claims against Schnitzer by cross-libel. The decree awards certain sums to Owners against Amtro, and certain sums to Amtro against Schnitzer, and directs that so much of the latter as necessary be applied to satisfy Owners' decree. This cross-appeal is directed to the failure of the decree in favor of Amtro against Schnitzer to award to Amtro certain additional sums sought by it, and to one item of the amounts awarded to Owners against Amtro.

The District Court had jurisdiction, by virtue of the constitutional grant of admiralty and maritime jurisdiction (Art. III, Sec. 2) and by virtue of 28 U.S.C.A. §1333(1), of all of the claims asserted in the libel and cross-libel as claims arising under and in connection with ship charters, which are maritime contracts, and as claims necessary to be resolved for a complete determination of the rights of the parties in a case where the first and fundamental exercise of the jurisdiction of the court is maritime. The District Court also had jurisdiction of all claims by Amtro against Schnitzer based on diversity of citizenship, 28 U.S.C.A. §1332(2), since Amtro is a corporation organized and existing under the laws of Panama, and Schnitzer is a corporation with its principal place of business in Portland, Oregon (Articles I and II of the Cross-Libel [R. Vol. I, p. 16] admitted in Articles I and II of Schnitzer's Answer [R. Vol. I, p. 27]).

The jurisdiction of this Court to review the said decree upon Amtro's Cross-Appeal rests upon the notice of appeal duly served and filed by Amtro on August 6, 1965 [R. Vol. I, p. 193] and upon 28 U.S.C.A. §§1291, 1294(1). No direct review by the Supreme Court may be had in this case.

Statement of the Case.

This case is a three-cornered controversy between the Owners of the cargo vessel S.S. Nictric, Amtro, as her time charterer, and Schnitzer as her voyage charterer. Amtro, by a time charter with owners, [Lib. Ex. 1, admitted R. Vol. II, p. 5] rented the cargo carrying capacity of the Nictric for a fixed period of time at a fixed monthly hire, the vessel continuing to be operated and maintained by the Owner with the Owner's master and crew, but at Amtro's directions as to employment. By voyage charter, [Lib. Ex. 2, admitted R. Vol. II, p. 5] Amtro sublet the carrying capacity of the vessel to Schnitzer, a large scrap metal dealer and exporter, for a single voyage carrying scrap steel from the Pacific Northwest to Japan, at a lump sum freight payable 90% in advance and 10% upon completion of discharge.

In the voyage charter, Schnitzer agreed to load, stow and discharge the cargo free of expense to Amtro, and to do so within a total of twenty-three (23) weather working days (usually called the "lay time") including time waiting for a berth. Schnitzer further agreed in the charter that if the vessel were "longer detained"

(without any time limit on this) Schnitzer would pay Amtro "demurrage" at the rate of \$700.00 per day.¹ This rate was less than the amount necessary to cover Amtro's expenses for the vessel during such detention. The charter also provided that "any extra expenses incurred by reason of nature of cargo" were to be for Schnitzer's account.²

The discharge in Japan was delayed for a period of nearly three months beyond the lay time due to congestion applicable to scrap cargos and the shortage of scrap discharge facilities at the port of Tokyo, Japan, to which Schnitzer sent the cargo.

During this long delay, the monthly hire of the vessel payable by Amtro to Owners kept accruing. Amtro demanded that Schnitzer pay the demurrage on a current basis. Schnitzer did not pay. After the vessel had been on demurrage for about one month, in response to a further demand by Amtro for payment of the demurrage, Schnitzer agreed to pay the demurrage, but objected to payment of the demurrage and the balance of the freight until completion of the discharge of the vessel on the ground that such items were not due under the charter until that time. Amtro threat-

¹The applicable provisions of the voyage charter [Lib. Ex. 2] (Schnitzer being "Charterer") were:

"17. Cargo is to be loaded, stowed and discharged by the Charterers, free of expense to the vessel.

"18. Cargo is to be loaded, stowed and discharged within a total of twenty-three (23) weather working days of 24 hours. . . . If longer detained, Charterers to pay demurrage at the rate stipulated in Clause 7 . . ."

"7. Demurrage, if incurred, to be paid by Charterers at the rate of seven hundred dollars (\$700) per day or pro rata for any part of a day."

"20. At each port, time to count . . . after due notice given, whether vessel in berth or not."

²Voyage charter [Lib. Ex. 2] clause 1.

ened to lien the cargo for the demurrage. Schnitzer took the position that under the charter Amtro had no lien on the cargo for the demurrage. Schnitzer persisted in this position toward Amtro until after the cargo had been discharged on December 31, 1961, and Amtro had lost whatever possessory lien on the cargo it might otherwise have had. At that point, Amtro demanded payment of the demurrage and freight from Schnitzer in accordance with the position Schnitzer had taken as to the date when it was payable. By this time, due to Schnitzer's failure to pay the demurrage, and the fact that Amtro could earn nothing from the operation of the vessel while it was waiting to discharge Schnitzer's cargo, Amtro had run out of funds and had fallen into default to Owners for time charter hire. Owners agreed however to waive the default if Amtro paid the arrearage promptly. When Amtro demanded payment from Schnitzer at the completion of discharge, Amtro advised Schnitzer that it needed payment of the demurrage in order to cure the default under its time charter with Owners, and that if the demurrage and freight were not paid, Amtro would be forced into final breach of its charter with Owners and would suffer damage as a result. Schnitzer refused to pay, and asserted thereafter, for the very first time, that it didn't owe the demurrage or freight at all because Amtro had failed to exercise a lien on the cargo. Schnitzer made this 180° reversal of position and refused to pay with full knowledge that this would ruin Amtro, and it did ruin Amtro. Since Schnitzer's action had made Amtro unable to reinstate the time charter, the Owners withdrew the vessel under the terms of the time charter effective December 31, 1965, and re-chartered her to another party, holding Amtro liable for damages.

Owners filed this action against Amtro for amounts due under the time charter and damages for its breach, and, by Writ of Foreign Attachment, attached all sums due from Schnitzer to Amtro. Amtro asserted its claims by cross-libel against Schnitzer. After trial, the District Court gave a decree in favor of Owners against Amtro for the amounts which it concluded were due from Amtro to Owners under the time charter, and for damages for breach of the time charter, consisting of the difference between the charter hire payable by Amtro for the balance of the term of the time charter remaining after Owners' withdrawal of the vessel less the amounts realized by Owners on a re-charter of the vessel to another party during a portion of that period. Amtro is appealing from that decree only in respect of one item of the amounts held to be due under the time charter.

The District Court gave Amtro a decree against Schnitzer for the demurrage and the unpaid balance of the freight under the voyage charter, with interest. We believe that the District Court was, beyond any doubt, correct in both its interpretation of the voyage charter and its findings of fact supporting this part of its decree. Amtro also claimed damages against Schnitzer for fraud in the inducement of the voyage charter. The District Court found the facts adversely to Amtro here, and although we believe that the Court weighed the evidence incorrectly, we must concede that the evidence on the material points was conflicting and that Amtro has no proper appeal to this Court on that issue. Amtro's Cross-Appeal with respect to the decree in its favor against Schnitzer is based on the failure of the District Court to include in that decree, in addition to the freight and demurrage, judgment for the sum of \$33,975.00

under the "extra expense" clause of the voyage charter, and judgment for the sum of \$24,745.27, plus interest, for which Amtro became liable to Owners for breach of the time charter because of Schnitzer's refusal to pay the demurrage on completion of the discharge.

Because of the complexity of this case, this statement has been a fairly general one. A further statement of the particular facts applicable to the points urged on this Cross-Appeal will be made in the argument. No attempt is made in this brief to state the additional facts which are material on the issues raised by Schnitzer's appeal.

Specifications of Error.

1. The District Court committed error of law in failing to include the amount of Amtro's liability to Owners for breach of the time charter (24,745.27 plus interest) in its decree in favor of Amtro against Schnitzer as damages for:

- a. Schnitzer's breach of the voyage charter contract, and
- b. Schnitzer's tort of intentional and unprivileged prevention of Amtro's performance of the time charter.

2. The District Court erred in failing to award to Amtro against Schnitzer the sum of \$33,975.00 under clause 1 of the voyage charter providing, "Any extra expenses incurred by reason of the nature of cargo . . . to be for charterer's account." The errors committed in this connection were:

- a. Error in construing the provision not to include extra expenses due to delay by reason of the nature of cargo [R. Vol. I, pp. 145-146].

b. Error in its finding of fact that “the record . . . does not support a finding that the total delay, or any specific part thereof, was due to the nature of cargo” [R. Vol. I, p. 145].

3. The District Court erred in construing the provision of clause 23 of the time charter, requiring Amtro to pay Owners “\$350.00 per month or pro rata in lieu of all over time,” to apply during the entire period of the time charter [R. Vol. I, pp. 133-134], rather than only during the loading and discharge of the vessel to which clause 23 related. This error rendered Owners’ judgment against Amtro for amounts due under the time charter excessive to the extent of \$1,179.94.

Summary of Argument.

I.

The \$24,745.27, plus interest, for which Amtro was held liable to Owners for breach of the time charter should have been awarded to Amtro against Schnitzer as damages both for Schnitzer’s breach of the voyage charter and for Schnitzer’s tort of intentional and unprivileged prevention of Amtro’s performance of its contract with Owners.

A. The actual cause of Amtro’s breach of its time charter was Schnitzer’s failure to discharge the vessel within the time provided in the voyage charter or to pay the demurrage. If Schnitzer had performed or paid, the breach of the time charter would not have taken place. The fundamental principle of the law of contract damages, namely to give compensation, to put the injured party in as good a position as if the contract had been performed, therefore requires the award of these damages.

The *Hadley v. Baxendale* rule generally limiting recovery of contract damages to those reasonably within the contemplation of the parties at the time when the contract was entered into does not forbid the damages in question. From the facts shown by unconflicting evidence to have been known to Schnitzer when the voyage charter was entered into, Schnitzer knew that a sufficiently serious breach of the voyage charter would cause damage of this type. Under the rationale of the rule, it should make no difference that, as the District Court found, the parties did not contemplate when the charter was entered into that the breach would be as great as it turned out to be.

In any event, the *Hadley v. Baxendale* rule should not be applied, in derogation of the overriding principle of compensation, where the reasons behind the rule do not support its application. The reason for the rule is that since a party who contracts usually assumes some risk that unforeseen circumstances may prevent or hinder his performance, it would unduly discourage the making of contracts if that party were held to a liability for failure to perform greater than that which he can foresee at the time he undertakes the obligation as likely to follow from non-performance. By paying the demurrage upon receiving notice from Amtro that non-payment would cause these damages to Amtro, Schnitzer could have limited its liability to no more than that which it expressly assumed in the event of its non-performance of its obligation that the vessel be discharged in time, namely the demurrage for the period of delay, however long. When the defaulting party to a contract has had, but has failed to take, this opportunity, there is no longer any reason for refusing to allow the injured party its full actual damages.

B. Schnitzer's refusal to pay the demurrage with knowledge that its failure to do so would disable Amtro from performing its time charter with owners was tort against Amtro as well as a breach of contract. The tort, recognized in admiralty as well as generally in the United States, was intentional interference with an existing contract relation (the time charter). The tort may be committed by acts which prevent one of the parties to a contract from performing it, financially or otherwise. It is actionable by the party prevented, and the damages include that party's liability to the other.

Under the admiralty decisions, as well as in the view advocated by the text writers, the tort is committed by an act which the actor knows will cause the breach, even though it is done for another purpose, unless that purpose and the means used are privileged. Schnitzer's refusal to pay was in that class, since its purpose, as far as appears from the record, was to postpone or avoid, if possible, the payment of the demurrage. The question of privilege is the question whether that purpose and the means used to advance it should be given protection by the law superior to the protection to which a party in Amtro's position is entitled. The purpose to avoid payment of a clear contractual obligation should create no privilege. If there is a privilege for the assertion of a bona fide (though mistaken) defense, Schnitzer cannot invoke it, since the only defense to payment urged by Schnitzer in the District Court (and presumably here) is based on an interpretation of the

voyage charter directly contrary to the charter interpretation urged by Schnitzer upon Amtro while the charter was in effect and at the time when Schnitzer refused to pay, and so prevented Amtro's performance of the time charter.

The District Court accordingly erred in denying these damages to Amtro, and its decree must be reversed in this respect, with direction to enter decree in favor of Amtro for these damages in addition to the demurrage and the balance of the freight.

II and III.

The issues on the extra expense clause of the voyage charter (Specification of Error 2) and the crew overtime clause of the time charter (Specification of Error 3) are, though important, so narrow in scope that a separate summary of our argument on these would, we believe, be more repetitive than helpful.

ARGUMENT.

I.

The District Court Erred in Failing to Award to Amtro Judgment Against Schnitzer in the Amount of Amtro's Liability to Owners for Breach of the Time Charter.

The District Court properly gave to Owners judgment against Amtro in the sum of \$24,745.27, plus interest, as damages for Amtro's breach of the time charter. The breach consisted in Amtro's failure to keep up the payments of time charter hire, as a result of which Owners withdrew the vessel under the time charter, effective on the completion of the discharge of the Schnitzer cargo. The damages awarded against Amtro consisted of the difference between the charter hire for the balance of the period of the time charter with Amtro and the amounts earned by Owners on a charter of the vessel to another party.

The undisputed evidence shows that the actual cause of Amtro's breach of the time charter and the damages suffered by Amtro therefrom in the form of judgment against Amtro by Owners was the failure of Schnitzer to discharge the vessel within the lay time provided in the voyage charter, coupled with the refusal of Schnitzer to pay the demurrage and the balance of the freight provided in the voyage charter. Until Schnitzer's cargo was discharged from the vessel, Amtro could, of course, not employ the vessel to earn any additional revenue. During the delay in discharge in Japan, Amtro's obligation to pay charter hire to Owners went right on. The operation of the Nictric under charter was at the time Amtro's sole business [R. Vol. II, p. 51]. Amtro's capital and the prepaid freight received on the Schnitzer charter

was sufficient to meet Amtro's charter hire payments and other expenses through November 7, 1961 [Pretrial Order, Admitted Facts IV, R. Vol. I, p. 103]. This was a month beyond the date when discharge would have been completed, and the vessel would have been available to Amtro for further employment, had Schnitzer discharged the vessel within the time promised in the voyage charter (The lay days expired October 9, 1961 [Pretrial Order, Admitted Facts X, R. Vol. I, p. 105]). Because of the unavailability of the vessel and Schnitzer's failure to pay the demurrage during the month of October, Amtro ran out of funds and was unable to pay the charter hire payment due November 7, 1961 [R. Vol. II, pp. 51-52]. The advance deposit of charter hire which Amtro had up with Owners was then applied to pay the charter hire through December 7, 1961 [Pretrial Order Admitted Facts IV, R. Vol. I, p. 103]. Amtro was without funds to pay charter hire beyond that point without payment of demurrage by Schnitzer. Since the non-payment was a breach of the time charter, Owners announced withdrawal of the vessel from Amtro, effective on completion of discharge, and stated their intention to hold Amtro liable for damages for the breach. Owners, however, announced themselves prepared to waive the default and reinstate the time charter if Amtro paid the amounts due under the time charter promptly following completion of discharge of the vessel.³

³Discharge was completed at midnight December 30-31, 1961, Japan time (December 29-30, 1961, U. S. West Coast time, due to the International Date Line). [Pretrial Order, Admitted Facts VIII, R. Vol. I, p. 105]. On December 31, 1961, Amtro received the following cable from Owners' New York brokers [Amtro Ex. 59 admitted R. Vol. II, p. 117]:

"In reply to your telegram 29th London cabled 30th quote Nictric owners quite prepared reinstate time charter pro-

The amount due under the time charter at that time, as found by the District Court, was \$23,689.30. The escrow deposit was a month's charter hire or \$24,629.50. The amount required to reinstate the time charter was therefore \$48,318.80. The amount of the demurrage and freight due and payable by Schnitzer on the completion of discharge was \$62,307.10, considerably more than enough to reinstate the time charter, including the deposit of one month's hire in advance. Therefore, if Schnitzer had paid the demurrage and balance of freight promptly after the completion of discharge, Amtro's breach of the time charter would have been avoided, and Amtro would not have become liable to Owners for the \$24,745.27 plus interest, in damages for that breach.

The undisputed evidence further shows that as the time for completion of discharge approached, and again when the discharge was completed, Amtro put Schnitzer on notice that if Schnitzer paid the demurrage and the balance of the freight a breach of Amtro's time charter would be avoided, and that if Schnitzer did not pay, the breach of the time charter with the resultant damage to Amtro would be inevitable.⁴ Schnitzer refused to pay in the face of that notice, and Amtro suffered the damages made inevitable thereby.

vided all outstanding moneys paid and further months hire deposited escrow stop. ETD tomorrow thence repairing ETC 8/10 January therefore subject unfixed other business Amtro have few days arrange finance unquote."

⁴The uncontradicted evidence shows that on December 26, 1961, Amtro's counsel sent the following telegram to Schnitzer [Amtro Ex. 60 admitted R. Vol. II, p. 116]:

"Re Nictric in our previous discussions you asserted that demurrage was payable upon completion of discharge and not before then stop. If you pay balance of freight and all demurrage owing on completion of discharge as you have contended it is payable Amtro will be able to cure its breach of its charter with owners stop. You are hereby given notice

Amtro's cross-libel against Schnitzer sought to recover these damages in addition to the demurrage and the balance of the freight. The District Court denied this recovery to Amtro. We contend that the District Court erred in so doing. Under the findings of the District Court and the uncontradicted evidence, the District Court should have awarded Amtro these damages for Schnitzer's breach of the voyage charter contract and for Schnitzer's tort of intentional and unprivileged prevention of Amtro's performance of the time charter.

A. The District Court Should Have Awarded Amtro These Amounts as Damages for Schnitzer's Breach of the Voyage Charter Contract.

The overriding principle and basic purpose of the law of contract damages is, as stated in

Williston, Contracts, Rev. Ed. 1936, vol. 5, p. 3763

"... to give compensation, that is to put plaintiff in as good a position as he would have been had defendant kept his contract."

This basic and overriding principle requires the award of these damages to Amtro for breach of contract, since if Schnitzer had either discharged the vessel within the

that if you do not pay all demurrage and unpaid freight promptly upon completion of discharge Amtro's charter will be incurably lost and Amtro will hold you liable for all loss and damage suffered by it thereby."

On January 2, 1962, Amtro's counsel sent the following further telegram to Schnitzer [Amtro Ex. 62 admitted R. Vol. II, p. 116]: "Nictic completed discharge Dec. 31 all demurrage freight now due payable stop. Owners have agreed reinstate charter if Amtro pays all sums due by Jan. 8 stop. Amtro can do so only if you pay demurrage freight by that date stop. If you do not pay Amtro holds you liable all damages arising from loss charter."

time in which it had contracted to discharge it or paid the demurrage, these damages would not have been suffered by Amtro.

The District Court denied these damages on the basis of a conclusion that they were not within the contemplation of the parties at the time the voyage charter was entered into. In so doing, the District Court obviously sought to apply what is commonly referred to as the rule in

Hadley v. Baxendale, 9 Exch. 341, 156 Eng. Rep. 145.

This rule, if carefully and properly analyzed in the context of the particular characteristics of the voyage charter as a contract, does not forbid Amtro's recovery. The District Court opinion, in the nature of Findings of Fact on this issue, states [R. Vol. I, p. 142]:

"After a complete analysis of the evidence before me, I do not believe that it would support a finding that either Amtro or Schnitzer contemplated the long delay which was incurred at the ports of discharge, nor could Schnitzer contemplate that its failure to pay demurrage would result in a withdrawal of the charter and consequential damages as herein fixed."

Since there is evidence to support it, although the evidence is conflicting, we must accept the District Court's finding that neither Amtro nor Schnitzer contemplated, at the time the voyage charter was entered into, the long delay which was incurred at the ports of discharge. We must take the second clause of the quoted finding to be dependent upon and a conclusion from the first, since, if it is not, it is clearly erroneous under the uncontradicted evidence.

The uncontradicted evidence demonstrates that Schnitzer knew when it entered into the voyage charter that Amtro was the time charterer of the vessel. The voyage charter with Schnitzer describes Amtro as "time chartered owner."⁵ A time charter, as its name implies, is always a charter at a fixed rate of hire based on time, and the hire continues no matter what the vessel is doing. Since Schnitzer's voyage charter was for the whole capacity of the vessel, it necessarily followed, and was known to Schnitzer, that until the cargo carried under the voyage charter was discharged, Amtro could earn no other income from the vessel with which to keep up the payments of the time charter hire. Schnitzer must have known from these facts that if Schnitzer failed *in a substantial enough degree* to fulfill its obligation in the voyage charter to discharge the vessel within the lay time provided in the voyage charter, and if Schnitzer then failed to pay the demurrage, it would follow in the ordinary course of things that Amtro would be forced into breach of its time charter and would become liable to owners in damages.

Concededly, this result was likely only if there were a long delay and a large demurrage obligation. The voyage charter, however, obligated Schnitzer to discharge the vessel within the twenty-three (23) weather working days, and provided that Schnitzer was to pay demurrage at the rate of \$700.00 per day "if longer detained."⁶ The voyage charter states no limit, and implies no limit, to the length of the detention for which Schnitzer is obligated to pay demurrage. In agreeing in a charter of this kind to discharge the vessel within a

⁵Voyage charter [Lib. Ex. 2] clause 1, line 1.

⁶Voyage charter provisions quoted in footnote 1 page 4.

fixed time, Schnitzer assumed the risk of *all* unforeseen circumstances which might prevent or delay discharge.

Empire Transp. Co. v. Philadelphia & R. Coal & Iron Co., 77 Fed. 919 (8th Cir. 1896);

St Ioannis Shipping Corporation v. Zidell Explorations, Inc., 222 F. Supp. 299 (D. Ore. 1963) *aff'd* 336 F. 2d 194 (9th Cir. 1964).

Therefore, Schnitzer assumed in this charter the risk of any delay, *however long*, and even if the discharge were delayed substantially forever, it would not relieve Schnitzer of the obligation it assumed. If Amtro's breach of its time charter should reasonably have been contemplated by Schnitzer as a result of a delay of any length, no matter how long, these damages were within Schnitzer's contemplation as likely to follow from a breach of the obligations it assumed in the voyage charter. A long enough delay could be expected to break any time charterer. These damages were therefore within Schnitzer's contemplation when it entered into the voyage charter.

To limit recoverable damages to those which could be contemplated as likely to flow from the *degree of breach* which the parties considered likely when the contract was entered into would make nonsense of the rule. When parties enter into a contract they ordinarily do not contemplate that it will be breached at all. Surely, under the rule in *Hadley v. Baxendale*, all damages are recoverable which are within the contemplation of the parties as a likely result of even a very large breach of the contract.

In any event, the rule in *Hadley v. Baxendale* should not be applied in view of the particular circumstances of this case. That rule is not, after all, a legislative en-

actment. It is a limitation worked out by the courts, in derogation of the general principle of awarding compensatory damages in contract cases, for particular reasons of policy. *It should not be applied when these reasons are not applicable.* The reasoning supporting the rule is that since a party who contracts usually assumes some risk that unforeseen circumstances may prevent or hinder his performance, it would unduly discourage the making of contracts if that party were held to a liability for failure to perform greater than that which he can foresee at the time he undertakes the obligation as likely to follow from some degree of non-performance. A typical statement of these considerations is found in one of the cases cited by the District Court,

Globe Refining Co. v. Landa Cotton Oil Co.,
190 U.S. 540, 543, 28 S. Ct. 754, 47 L. Ed.
1171 (1902).

Ordinarily these considerations are unchanged by the fact that notice of the damages which will flow from a breach is given to the party after the contract is made but before the time for performance arrives, since at that time the party to whom notice has been given may still be unable to deliver the promised performance, and to hold him for damages on the basis of notice at that time will still increase his risks beyond those which he knew or ought to have known he was assuming when he entered into the contract. This is the reason why, as Justice Holmes observed in the *Globe Refining Co.* case:

"The suggestion thrown out by Bramwell, B., in *Gee v. Lancashire & Yorkshire Ry. Co.*, 6 H. & N. 211, 218, that perhaps notice after the contract was made and before breach would be enough, is not accepted by the later decisions."

These policy considerations in no way support a denial of the damages sought by Amtro under the particular facts in this case. The risk expressly assumed by Schnitzer in the voyage charter was the risk that unforeseen circumstances would prevent discharge of the vessel within the time provided, and that Schnitzer would have to pay demurrage for that time, no matter how long it might be. When Amtro gave Schnitzer notice of the consequences that would follow from non-payment of the demurrage, Schnitzer had the opportunity to avoid these consequential damages by paying the demurrage. By paying at that time, Schnitzer could have held its liability for the delay in discharge to exactly the liability which it expressly assumed in the charter, namely the demurrage, however much it might be. Schnitzer chose not to avail itself of that opportunity. There is no evidence in the record to show or suggest that Schnitzer was unable to pay the money, had it chosen to do so, and Schnitzer has never contended in this case that it was unable to pay due to unforeseen circumstances or otherwise. Since Schnitzer was given the opportunity to limit its liability to that assumed by the express terms of the charter, and did not choose to avail itself of it, the reason for the rule in *Hadley v. Baxendale* is not violated by allowing to Amtro the damages actually caused to Amtro and actually known to Schnitzer when it rejected this opportunity. The rule should therefore not be applied to prevent the award of fully compensatory damages in this case.

Looked at from a slightly different vantage point, what Schnitzer did by rejecting this opportunity was to refuse, when it could reasonably have done so, to mitigate the damages flowing to Amtro from Schnitzer's

breach of its charter obligation of timely discharge of the vessel. If the party injured by a contract breach has a duty to act reasonably to mitigate its damages, the party breaching the contract must have at least an equal duty. As stated in,

14 California Jurisprudence 2d, pp. 731-2.

“In the event of a breach of contract, the parties are *mutually* obligated to mitigate the damages stemming from the breach; . . . (emphasis added)”

We have been unable to find any authority applicable to the situation presented in this case which would be binding upon this court. The closest analogy we have found to the problem of contract damages presented in this case is that considered by the Supreme Court of Texas in

Bourland v. Choctaw, O. & G. Ry. Co., 99 Tex. 407, 90 S.W. 483 (Supreme Court of Texas 1906).

In that case plaintiff was fattening beef cattle for market. Anticipating that his supply of feed would soon be exhausted, he purchased two carloads of feed and delivered them to defendant Railway to be carried to his feed lot. No notice was given to defendant at that time of the purpose for which the cake was needed, nor of the damage which would result from delay in delivering it. On the day on which the railroad cars reached their destination, plaintiff applied to defendant's station agent for delivery of the shipment, and stated to defendant's agent at that time that plaintiff was out of feed and that plaintiff had to have the feed to feed his cattle. After receiving this notice, defendant failed to make delivery, and by some mistake the cars were

sent out on another railroad and were not recovered. The feed was not delivered until nearly a month later. The jury awarded the plaintiff damages based on the depreciation in value of plaintiff's cattle caused by the lack of feed. The intermediate appellate court reversed on the basis of the Texas decisions applying *Hadley v. Baxendale*. The Supreme Court of Texas reversed the intermediate court and affirmed the judgment of the trial court awarding the damages. It reasoned as follows:

“The Court of Civil Appeals felt constrained by the decisions of this court in the case of *Missouri, Kansas & Texas Railway Company v. Belcher*, 88 Tex. 549, 32 S.W. 518, Id., 89 Tex. 428, 35 S.W.6, Id., 92 Tex. 593, 50 S.W. 559 to hold that damages of the character claimed were not recoverable, because notice of the peculiar state of facts under which they might arise as a consequence of delay in the transportation and delivery was not given to the defendant before or at the time of the making of the contract of carriage. It is true that the statement, in *Hadley v. Baxendale*, and in the many cases following it, of the rule for the recovery of damages of a special or exceptional kind for the breach of a contract for the delivery of property, includes, as essential to liability therefor, notice, at the time of the making of the contract, to the party bound to deliver, of the peculiar conditions under which such damages are likely to result from the breach; and the formula seems sometimes to have been applied as rigidly as if it were a rule prescribed by legislative act. Its operation has generally been wise and just, and it is only

when it is made the exclusive rule in cases in which the reasons underlying it do not make it applicable that it fails to meet the demands of substantial justice. . . .

In most of the decisions the question as to the exact time when the notice should have been given has not received much attention; there being no difficulty arising from the fact that it was given after the contract was made, but before the damage resulted. But in some cases it has been attempted to establish the right to damages beyond those which would ordinarily arise from the breach of the contract in the particular case, by showing notice of the special circumstances after the making of the contract and before the breach, and, although there was an intimation by one of the judges in *Gee v. L. & V. Ry. Co.*, 6 H. & N. 217, that such notice ought to be held to be effectual for the purpose, the decisions have been to the contrary in cases of this character which have come to our attention, where it became necessary to pass upon the point. *Jordon v. Patterson*, 67 Conn. 473, 35 Atl. 521; *Ligon v. Mo. Pac. Ry. Co.*, 3 Willson, Civ. Cas. Ct. App. §1; 1 Sedgwick on Damages, §158. The principle of these decisions is that the party undertaking the delivery is held to assume, when he makes his contract, a liability only for those damages which would, in the usual and ordinary course of things, result from his failure to perform, because it is only these that he is required to foresee, unless it is shown that knowledge of an unusual situation of the other party, in which extraordinary injury may be caused by nondelivery, has been brought to his attention,

and that he has contracted with reference thereto. In other words, it is held that the rights and liabilities of the parties are fixed by the contract and the circumstances known to them when it is made, and cannot be increased by notice of other facts subsequently given. The reasons which have been given for this are well condensed by Judge Denman in the *Belcher Case*, 89 Tex. 428, 35 S.W. 6. The notice relied on in such cases subsequent to the contract appears to have been given at a time when its effect, if held sufficient, would have been to impose an additional liability, resulting from the contract itself, to that within the contemplation of the parties when they made it. In none of them were the facts like those in the present case, in which the contract to carry to Washita had been fully performed, and the property was at the point of destination, and could have been delivered, when the notice was given. All that remained to be done was to make delivery, and this it was then in the power of the carrier to do at once. It had no right to demand extra compensation for a transportation already performed, for making delivery; nor had it the right to refuse or delay delivery because of the conditions of which it then received notice. No extra or unusual preparations were necessary for delivery, or, if they were, the defendant was, at the time, in as good a position to make them as it would have been, had the notice been given when the contract was made. The simple fact is that it held so much of plaintiff's property of which he desired, and was entitled to immediate possession, for a special purpose and for the lack of which, de-

fendant was then fully informed plaintiff was in danger of suffering the loss for which compensation is now sought, which loss could have been prevented by mere delivery of the property. In such a case, knowledge of these facts, when the contract for transportation was made, appears to us to be unessential. None of the reasons exist for which such notice has been required in other cases. The plaintiff's loss did not arise from delay in transportation, nor from any cause for the prevention of which notice at the time of the contract was important, but from the failure to perform the simple duty to deliver the property, due to the faithlessness of defendant's agent, at a time when the probable consequences thereof were fully disclosed."

The reasoning of the Texas court in that case for awarding the consequential damages to the plaintiff exactly supports Amtro's recovery in this case. All that remained to be done by Schnitzer at the time that Schnitzer received notice that failure to do it would damage Amtro was to make payment. Schnitzer did not have the right to refuse payment. Amtro's damages, in the words of the *Bourland* decision, "did not arise from . . . any cause for the prevention of which notice at the time of the contract was important, but from the failure to perform the simple duty to [pay the demurrage and balance of the freight] at a time when the probable consequences thereof were fully disclosed."

There is no valid reason why the fact that the duty involved in the present case was the duty to pay money rather than the duty to deliver property, as in the *Bourland* case, should make any difference in the prin-

ciple to be applied. This is not a situation coming within the old maxim that for mere delay in paying a money demand, interest on the money is the only damages to be recovered. This court has recognized that this rule is not applicable "where the obligation to pay is special and has reference to objects other than the mere discharge of a debt."

Hasquet v. Big West Oil Co., 29 F. 2d 78, 79
(9th Cir. 1928).

Schnitzer's demurrage obligation was in this excepted category. Schnitzer's fundamental obligation under the voyage charter was that the vessel should be discharged, and hence available for other employment by Amtro, within the lay time. The demurrage was merely a stipulated payment to be made by Schnitzer to Amtro for breach of this primary obligation. It was primarily of advantage to Schnitzer, since, under evidence as to which there is no conflict (see p. 46 of this brief), the stipulated demurrage rate was substantially less than the expenses which would actually be suffered by Amtro during any period of delay. A contract such as this charter was cannot be treated as simple obligation to pay money. It would be entirely unreasonable to hold that the damages payable by Schnitzer for the breach not only of its secondary demurrage obligation, but also of its primary obligation to discharge the vessel in time, are the amount of the secondary obligation, plus interest, where Schnitzer refused to pay the secondary obligation at a time when Schnitzer knew that payment was required to avoid consequential damages to Amtro.

Because of the particular dual nature of Schnitzer's obligation under the voyage charter, it is not necessary that this Court in this case re-examine the basic prem-

ises behind the rule making the amount of the debt plus interest the exclusive measure of damages for failure to pay a simple debt. We submit, however, that this rule is over-ripe for re-examination in the light of modern conditions and developing concepts of business morality. The rule, though an ancient one, has never been justified on any grounds higher than convenience. *Williston on Contracts*, Vol. 5, page 3925, states the justification as follows:

“The universality of the rule limiting damages to interest in thus based on a policy of having a measure of damages of easy and certain application, even if it occasionally leads to results at variance with the general principle of compensation.”

Under modern conditions any universal and automatic application of the rule leads to evils which far outweigh any convenience of the rule. If the rule is universally applied, it provides an incentive for any business man who is able to earn more than the legal interest rate by using his money in his business (and this includes almost all business men under present conditions) to refuse to pay his debts, whether he has any meritorious defense or not, simply for the sake of the continued use of the money while the claim is being tried through the courts. This furnishes a strong temptation to the unscrupulous to engage in tactics which the business community recognizes, and should recognize, as unethical. From the point of view of the administration of the courts, it would seem that the burden of the unmeritorious litigation which the rule tends to produce far outweighs any convenience in the determination of damages which is provided by the rule. Certainly justice requires the allowance of damages in addition to the

interest in any case where defendant was placed on notice at the time payment was due that his failure to pay would cause such damages, and chose to refuse to pay nevertheless.

For all of the foregoing reasons, the District Court should have awarded to Amtro against Schnitzer, in addition to the demurrage and the balance of the freight and interest thereon,⁷ consequential damages for Schnitzer's breach of the voyage charter contract in the amount of Amtro's liability to Owners for the time charter breach.

B. The District Court Should Have Awarded Amtro These Amounts as Damages for Schnitzer's Tort of Intentional and Unprivileged Prevention of Amtro's Performance of the Time Charter.

Even if, despite the foregoing, these damages must be held not to be recoverable by Amtro as consequential damages for breach of contract, they should have been awarded to Amtro as tort damages against Schnitzer. Under the facts shown by the uncontradicted evidence and the findings of the District Court, Schnitzer's act in refusing to pay the demurrage to Amtro after notice of, and in wilful disregard of, the consequences to Amtro was a tort.

⁷There is no element of double recovery here, since if Schnitzer had paid the demurrage and the balance of freight, Amtro would have had the use of the money and would also have avoided liability to Owners for damages for breach of the time charter. Amtro would have used part of the money from Schnitzer to pay the amounts then due to Owners under the time charter (in distinction to the damages for its breach), but the District Court has in its present judgment allowed interest on those amounts to Owners against Amtro at the same rate as the interest allowed Amtro against Schnitzer on the demurrage and the balance of the freight.

The law is clear that if a breach of contract is also a tortious breach of a duty owed by the defendant to the plaintiff, tort damages may be allowed. An act that constitutes a breach of contract may also be tortious.

Acadia, California, Ltd. v. Herbert, 54 Cal. 2d 328, 5 Cal. Rptr. 686, 353 P. 2d 294 (1960);

Jones v. Kelly, 28 Cal. 251, 255-56, 280 Pac. 942, 943 (1929);

Harper v. Interstate Brewery Co., 168 Or. 36, 120 P. 2d 757, 762-763 (1942);

Peitzman v. City of Illmo, 141 F. 2d 956 (8th Cir. 1944), cert. den. 323 U.S. 718, 89 L. Ed. 577, 65 S. Ct. 47, reh. den. 323 U.S. 813, 89 L. Ed. 647, 65 S. Ct. 112;

Sanderson v. Crowley, 180 F. 2d 124 (5th Cir. 1950).

The duty to Amtro which Schnitzer breached was the overriding duty which every man owes to another not to intentionally injure him. That the duty grew out of a contract does not make its breach any less a tort. As the California Supreme Court stated in *Jones v. Kelly*, *supra*:

"If the cause of action arises from a breach of promise, the action is ex contractu, but, if it arises from a breach of duty growing out of the contract, it is ex delicto. *Mobile Life Ins. Co. v. Randall*, 74 Ala. 170. A tort and trespass is none the less such because it incidentally involves a breach of the contract. *Stock v. Boston*, 149 Mass. 410, 21 N.E. 871, 14 Am. St. Rep. 430. The law imposes the obligation that 'every person is bound, without contract, to abstain from injuring the per-

son or property of another, or infringing upon any of his rights.' Section 1708, Civ. Code. This duty is independent of the contract and attaches over and above the terms of the contract."

Or as the Oregon Supreme Court stated in *Harper v. Interstate Brewery Co.*, *supra*:

"Thus it may be necessary for a plaintiff to show a contract between himself and the defendant in order to establish that the defendant has assumed a position, relationship or status upon which the general law predicates a duty independent of the terms of the contract but it does not necessarily follow that his only remedy is *ex contractu*. If from the position, contractually assumed, a duty be raised independent of the contract an action in tort may lie."

Such an additional element of duty may be raised by notice of special circumstances brought home to the obligor under a contract at the time performance is due, the duty being to act reasonably in the light of those circumstances.

Gardner v. Mid-Continent Grain Co., 168 F. 2d 819 (8th Cir. 1948).

See also:

Conn v. Texas & N.O. Ry. Co., 14 S.W. 2d 1004 (Comm. of Appeal of Texas 1929);

Western Union Telegraph Co. v. Hice, 288 S.W. 175 (Comm. of Appeal of Texas 1926);

Virginia-Carolina Peanut Co. v. Atlantic Coast-line Railroad, 155 N.C. 148, 71 S.E. 71 (1911).

The tort committed by Schnitzer against Amtro was the tort of intentional and unjustified interference with Amtro's contract with owners. This tort is recognized under federal law, see

Arkansas v. Texas, 346 U.S. 368, 74 S. Ct. 109, 98 L. Ed. 80 (1953).

and is recognized as a maritime tort for the purposes of admiralty jurisdiction when the contract interfered with is a maritime contract.

Sidney Blumenthal & Co. v. United States, 30 F. 2d 247 (2d. Cir. 1929) cert. den. 279 U.S. 847, 73 L.Ed. 991, 49 S. Ct. 345;

The Poznan, 276 Fed. 418, 433 (S.D.N.Y. 1921, L. Hand, D.J.).

The tort may be committed by acts which disable one of the parties from performing his contract just as much as by the act of inducing a breach.

Angle v. Chicago, St. Paul etc. Railway, 151 U.S. 1, 13-15 (1893), 38 L. Ed. 55, 14 S. Ct. 240 (in which disablement was stated to be an *a fortiori* instance of the tort);

Sidney Blumenthal & Co. v. United States, cited *supra*;

The Poznan, cited *supra*;

Bacon v. St. Paul Union Stockyards, 161 Minn. 522, 201 N.W. 326 (1924).

Acts disabling a party to a contract from meeting his financial obligations under the contract are a basis for the tort just as much as acts disabling the party from performing in any other way.

Keene Lumber Co. v. Leventhal, 165 F. 2d 815 (1st Cir. 1948) (acts by defendants in diverting from a corporation the assets needed to meet its debts held to be a tort as to a creditor of the corporation whose claim the corporation was thereby rendered unable to pay).

See also:

Angle v. Chicago, St. Paul etc. Railway, cited *supra* (in which plaintiff had contracted with a railway company to build a stretch of railway, and defendants wrongfully procured the revocation of a land grant to the railway company. Plaintiff was held entitled to recover damages in tort on the basis of defendant's unprivileged interference with the contract between plaintiff and the railway company, a portion of which damages arose from the fact that the railway company was thereby deprived of the means to pay plaintiff under the contract).

Many of the cases involving this tort have arisen as suits by one of the parties to a contract against a third party who interfered with the performance of the other party to the contract. However, the tort recovery is not limited to these situations. If the party whose own performance is interfered with is the party damaged, that party is equally entitled to damages in tort for the injury suffered.

Wilkinson v. Powe, 300 Mich. 275, 1 N.W. 2d 539 (1942);

Lichter v. Fulcher, 22 Tenn. App. 670, 125 S.W. 2d 501 (1938);

Prosser, Torts, 3rd Ed. p. 960.

“We may generalize that any intended and unprivileged interference which causes loss to either party to a transaction is actionable by the party suffering the loss.”

Harper and James, Law of Torts (1956), Vol. 1, p. 499.

In the present case, that it was Amtro rather than owners which were damaged by Schnitzer's acts disabling Amtro from performing its contract with owners does not alter the principles involved. This is nicely illustrated by two cases arising out of the same set of facts,

Knickerbocker Ice Co. v. Gardiner Dairy Co.,
107 Md. 556, 69 Atl. 405 (1908).

and,

Sumwalt Ice Co. v. Knickerbocker Ice Co., 114
Md. 403, 80 Atl. 48 (1911).

the first of which is one of the landmark cases in this area of tort law. In those cases, Knickerbocker Ice Co., which was an ice manufacturer, contracted with Sumwalt Ice Co., which was a dealer, to supply all of Sumwalt's ice requirements for a specified period. Sumwalt Ice Co. contracted with Gardiner Dairy Co. to supply ice to Gardiner Dairy Co. Knickerbocker informed Sumwalt that it would stop selling to Sumwalt, despite its contract with Sumwalt, if Sumwalt did not breach its contract with Gardiner and stop selling to Gardiner. Sumwalt, under pressure of this threat, did stop selling to Gardiner, and Gardiner was thereby forced to buy ice direct from Knickerbocker at a higher price. In *Knickerbocker Ice Co. v. Gardiner Dairy Co.*, Knickerbocker was held liable to Gardiner for the damages caused to Gardiner by Knickerbocker's tortious in-

terference with the contract between Gardiner and Sumwalt. In *Sumwalt Ice Co. v. Knickerbocker Ice Co.*, a separate suit, Sumwalt was held entitled to recover from Knickerbocker the damages suffered by Sumwalt from the loss of its contract with Gardiner because of the same tortious interference.

These cases also illustrate that the tort of unjustified interference with contractual relations is no exception to the general rule that conduct which is a breach of contract may also be a tort. The act of Knickerbocker which was held to be a tort as to both Sumwalt and Gardiner was a threat by Knickerbocker to breach its contract with Sumwalt. Indeed, one of the grounds upon which the court in *Knickerbocker Ice Co. v. Gardiner Dairy Co.* held that Knickerbocker's threat to Sumwalt was tortious was that the threat was not within Knickerbocker's rights under the terms of the Knickerbocker-Sumwalt contract.

A negligent, as distinct from an intentional, interference with a contract is generally held not actionable. On the other hand, malice in the sense of a desire to harm the plaintiff is not a necessary element of the tort. In many of the cases, the object of defendant's interference with the contract was to appropriate the benefits of the plaintiff's business to himself, and where this is the objective, it is generally held that the interference is actionable even though the defendant would have had the right to do what he did had he not done it for this purpose.

See, *e.g.*,

Knickerbocker Ice Co. v. Gardiner Dairy Co.,
cited *supra*, at page 409 of 69 Atl.;

Wilkinson v. Powe, cited *supra*.

It has also been held, however, that the party interfering with the performance of the contract may be liable in tort for the resulting damages where he has interfered in pursuit of his own ends, unrelated to the prevention of performance, but with the knowledge that his conduct is certain or substantially certain to prevent performance of the contract. The question determinative of liability in that situation is the question of whether the defendant was privileged to do what he did, that is to say whether the objective pursued by the defendant and the means used are ones to which the law should give protection superior to the protection afforded to the interest of the plaintiff in the contract which was interfered with. Though there is some conflict in the decisions involving that situation, this is the view favored by the leading text writers on torts.

See:

Prosser, Torts, 3rd Ed. pp. 966-67;

Harper and James, Law of Torts, 1956 Ed., Vol. 1, pp. 497-8.

This is also the clear holding of the two admiralty cases which we have found involving this tort. In

Sidney Blumenthal & Co. v. United States, cited *supra*,

the U. S. Fleet Corporation issued a bill of lading to the libelant for the carriage of goods belonging to the libelant from Shanghai to Seattle with trans-shipment to New York. The bill required the goods to be trans-shipped at Seattle on a ship of one of two specified lines. The managing agents for the vessel on which the goods were carried from Shanghai to Seattle, with knowledge of the terms of the bill of lading, trans-

shipped the goods at Seattle upon a steamer of another line, which became a total loss. The libelant cargo owner was held entitled to recover from the U. S. Fleet Corporation for the loss of the goods on the ground of conversion consisting of a violation of the trans-shipment terms of the bill of lading. The U. S. Fleet Corporation had impleaded the managing agents asserting liability-over. The U. S. Fleet Corporation was held entitled to recover from the managing agents the amount for which the U. S. Fleet Corporation became liable to the libelant for breach of the bill of lading contract. (It should be noted that this is precisely the same arrangement of the parties and precisely the same type of relief which is being sought by Amtro against Schnitzer in this case.) The Court of Appeals for the Second Circuit held the managing agent liable on the ground that it had committed the tort of unprivileged interference with the performance by the U. S. Fleet Corporation of its bill of lading contract with libelant. This was not a case in which the managing agent brought about the breach of the contract with the object of profiting from the breach. The basis of the managing agent's tort liability was only that it had trans-shipped with knowledge that this would cause a breach of the bill of lading contract, and without any interest in doing so which could form the basis for any privilege to do so. The reasoning of the court on this issue, as stated in the opinion by Judge Learned Hand, was as follows:

“ . . . but the question of ‘malice’ is more difficult. In the earlier cases the courts generally added that ‘malice’ or some unlawful means was an essential element to the liability. [citing cases] The notion may be found in more recent cases [citing cases], though it is usual, when any motive is re-

quired, to define it as a purpose to profit at the promisee's expense [citing cases]. But there is a substantial body of authority saying that the liability depends upon the actor's intention to cause the breach, which puts upon him the duty to show some excuse or justification. [citing cases] Perhaps it would be untrue to say that the doctrine has as yet come to rest, but it seems probable that, when the wrong is in procuring the breach of an existing contract, as distinct from interfering with the plaintiff's business or trade, motive will in the end disappear as a constituent element, though it may indirectly be material.

The first step was to recognize that a promisee had any rights, except as against the promisor. That bridge crossed, and the person who induced or made inevitable the breach being recognized as a tort-feasor, there seems to be no reason for treating the tort as different from any other. Conduct which produces a loss may of course be privileged; that is to say, the actor may be asserting or protecting some interest which the law admits as an excuse, and his motive is at times relevant. Perhaps this is merely because it is thought reprehensible, though the more satisfactory reason is that his purpose may disclose that he is not genuinely engaged in asserting the protected interest, in which case no conflict really arises between it and the interest of the injured party. But, if he have no interest to assert, he can have no privilege and his motive can hardly be material."

The other admiralty case which we have found, decided by Judge Learned Hand as District Judge, is

The Poznan, cited *supra*.

That case involved a vessel under charter. The charterer, not as agent for the owner or master but in its own name, issued bills of lading for the carriage of cargo from New York to Havana. Since the congestion in the Port of Havana was extreme, the owners of the vessel, instead of permitting it to wait and discharge the cargo, ordered it back to New York. They thereby made it impossible for the charterer to perform its bill of lading contract with the shipper. The owner was held liable to the shipper in tort for damages for the non-delivery on the ground that the action of the owner was an unprivileged interference with the performance of the bill of lading contract. The owner was not in any position to profit from the breach of the bill of lading contract as such. The owner's interest was in avoiding its own expense in having a vessel idle at Havana, under a charter to a charterer in financial difficulties.

The same principle was applied by the Court of Appeals for the First Circuit (under Massachusetts law in this instance) in

Keene Lumber Co. v. Leventhal, cited *supra*.

In that case, the interest being served by the parties who diverted the assets from the corporation was their own profit in doing so, not any interest in the breach of the corporation's obligation to plaintiff which was caused thereby. The acts of the defendants were held to be a tort as to the plaintiff creditor of the corporation on the ground that these acts were committed with knowledge that they would cause breach of the corporation's obligation to plaintiff, and were not privileged because the means used were wrongful.

Under these principles, Schnitzer, having refused to pay Amtro at a time when it knew that its refusal to

pay would disable Amtro from living up to its time charter with owners, is liable in tort to Amtro for the damages caused thereby unless Schnitzer can rely upon some privilege which the law should recognize as superior to Amtro's interest. We have found no precedent on the question of privilege in this setting. The interest being served by Schnitzer was, as far as appears from the record, its interest in delaying payment of a clear and unambiguous obligation, perhaps because it could use its money more profitably somewhere else in the interim. In all justice, it is hard to see how this can be a basis for any privilege in the face of the severe and known damage to Amtro. Perhaps even in the face of the known damage to the other party, a party to a contract should be privileged to refuse payment in order to assert what it believes in good faith to be a defense to payment. Even here, however, it could be argued with great force that if a party should choose to rely on such a defense in the face of known damage to the other party, the party so relying should be required to do so at his peril to the extent that, if the court subsequently holds the defense to be groundless, the party should be required to pay the compensatory damages.

This Court does not have to resolve that difficult question in this case. The facts found by the District Court clearly establish that when Schnitzer received notice that failure to pay would disable Amtro from performing its time charter with owners, and refused to pay in the face of that notice, it did not do so for the purpose of asserting any good faith defense to liability. The defense to liability finally asserted by Schnitzer in the District Court, (and upon its appeal to this Court),

is based entirely on the assertion that the voyage charter required Schnitzer to pay the demurrage and the balance of the freight only if Amtro was unable to obtain payment by exercising a lien on the cargo, and that Amtro was in fact able to obtain payment by this means. The foundation for this defense by Schnitzer is an interpretation of the charter *directly opposite* to the interpretation which Schnitzer adopted and urged upon Amtro at all times while the charter was in effect, and until after the completion of the discharge, including the time at which Schnitzer received notice from Amtro that payment was needed in order to prevent breach of the time charter. The District Court found this to be the fact. Its finding was as follows [R. Vol. I, pp. 140-141]:

“Aside from the views here expressed on the interpretation of the charter, I find a record which places Schnitzer in the indefensible position of first agreeing to pay demurrage, and later attempting to change its position. On November 13, 1961, when Schnitzer was first contacted by Amtro’s counsel, after the vessel had been on demurrage for about one month, Schnitzer agreed to pay the demurrage, but objected to payment of that item and the balance of the freight until the completion of the discharge, on the ground that such items were not due under the charter until that time. This testimony of a Mr. Fletcher is uncontradicted. Subsequently, Schnitzer’s counsel took the position that in fact there was no lien on the cargo for the demurrage. Schnitzer relied on this construction of the contract from about November 17th until after the cargo had been discharged on December 31st.”

Under these facts found by the District Court, Schnitzer has no possible privilege, and Schnitzer's refusal to pay the freight and demurrage after notice was an unjustified prevention by Schnitzer of Amtro's performance of its time charter contract with owners, and therefore a tort by Schnitzer. Amtro is entitled to recover from Schnitzer for that tort the damages caused thereby to Amtro, consisting, in addition to the demurrage and balance of freight and interest thereon, of the damages payable by Amtro to owners for breach of the time charter, including of course the interest which has been allowed owners against Amtro on those damages.

On all of the grounds stated, the judgment of the District Court must be reversed insofar as it denies these damages to Amtro, with directions to enter judgment for these damages.

II.

The District Court Erred in Failing to Award to Amtro Against Schnitzer the Sum of \$33,975.00 Under the "Extra Expense" Clause of the Voyage Charter.

The voyage charter between Amtro and Schnitzer [Lib. Ex. 2], in addition to the provisions requiring the vessel to be loaded and discharged within the lay time and the demurrage provision, contained the following provision in clause 1 as part of the typewritten language specifying the types of cargo to be carried for Schnitzer:

"Any extra expenses incurred by reason of nature of cargo and of metallurgical expert to be for charterers' account."

Evidence was introduced at the trial as to which there is no conflict whatever that the delay to the *Nictric* in obtaining a berth in Japan and discharging was due to the fact that she carried scrap cargo of the particular nature which Schnitzer loaded aboard her, and not other cargo, and that during the period of delay thus caused Amtro's expenses exceeded the demurrage rate by the sum of \$450.00 per day, for a total of \$33,975.00. Amtro sought to recover this amount from Schnitzer as "extra expense" under the above clause. The District Court denied Amtro recovery on the basis of the following interpretation of the charter clause [R. Vol. II, pp. 145-146]:

"Furthermore, it would require the imagination of a leprechaun to extend this language to cover a situation where a ship carrying scrap was compelled to wait longer to obtain a berth than ships carrying other kinds of cargo. Obviously, the 'extra expenses' mentioned in this clause refer to those expenses, if any, directly incurred in loading, transporting or discharging the scrap."

Without claiming any relationship to Irish elves, we submit that this interpretation of the clause restricts its application in a way not warranted by its language. The clause does not say "directly" incurred, and makes no reference to the loading transporting or discharging of the scrap, or to any other category of expenses. The clause states, without qualification, "any extra expenses incurred by reason of nature of cargo."

If this Court believes that the clause is ambiguous in this respect, such ambiguity must be resolved against

Schnitzer in view of the following Finding of Fact of the District Court [R. Vol. I, p. 140] :

“The form of the contract, the language used, the deletions made and the endorsement attached, are all chargeable to Schnitzer and, I so find under the undisputed evidence before me.”

It is true that the demurrage provision in this charter specified an amount to be paid by Schnitzer for each day by which Schnitzer failed in its obligation to load and discharge the vessel within the lay days. However, this was for delay generally and without regard to cause. It did not purport to rule out or supersede other clauses in the charter providing for payment of additional expenses from particular causes, even though these causes might involve delay as one of their elements. This is particularly clear in this charter where the demurrage rate was fixed at a figure far less than Amtro's expenses of operating the vessel during any period of delay, and therefore was not designed, as the District Court characterized it, “to make an adequate allowance or compensation for the delay or detention of the vessel” [R. Vol. I, p. 146].

The District Court made the following Finding of Fact on this issue [R. Vol. I, p. 145] :

“While the record discloses that a scrap cargo, such as was carried by the NICTRIC was not favored in the discharging scheme in Japan, it does not support a finding that the total delay, or any specific part thereof, was due to the nature of the cargo.”

The second part of this finding is clearly erroneous under evidence as to which there is no conflict in the

record. Pacific Marine Corporation, Schnitzer's Tokyo agent under this charter [Pretrial Order, Admitted Facts XII, R. Vol. I, p. 106] prepared a report on the congestion dated September 15, 1961, which was admitted into evidence as Exhibit F-23 to the depositions taken in Japan. This report was properly admitted into evidence by the District Court as a business record [R. Vol. I, p. 186]. The date of the report was while the Nictric was at the port of Tokyo waiting for a berth.

The report states, as to the congestion:

“II. Present Position:

(A) Degree of Congestion

The degree of congestion depends in large measure on the type of cargo being carried and we would list the types of operation in order of increasing congestion as follows:

- (1) Regular liner vessels loading general cargo at all ports—very little congestion except at individual ports on occasional month-end dates.
- (2) Regular liner vessels discharging general cargo with no more than 3,400 tons of non-ferrous scrap—comparatively little congestion, possibly 2 or 3 days delay altogether in Japan.
- (3) Semi-liner vessels including larger quantities of non-ferrous or ferrous scrap—one or two weeks slowdown at each port.
- (4) Tramp vessels discharging ore, coal, grain or other commodities going into consignees' own installation or into 'clean cargo' lighters—one week or so delay.

- (5) Tramp vessels discharging [sic] lumber, logs (into the water) or scrap into 'dirty cargo' lighters—great congestion ranging from one week to three months' wait for berth and three weeks to one-and-a-half months for discharge.

(B) Commodities

The worst commodities are scrap, then lumber, logs."

The testimony of Mr. Saishoji, the head of Tokyo Operations of the tramp ship agency division of owners' agents in Japan [Ex. 44E, p. 36, lines 1-23], the testimony of Leonard Schnitzer [R. Vol. II, p. 190] and the testimony on deposition of Mr. Koizumi, a manager of Pacific Marine Corporation called as a witness by Schnitzer at the depositions in Japan [Ex. 44H, pp. 187-26 to 187-27] was to the same effect and corroborate the report.

Moreover, the District Court made a finding of fact in another connection from which it follows that the particular nature of the Nictric scrap caused the delay. Schnitzer contended at the trial that Amtro could have liened the cargo by discharging it at a special wharf it contended was available. The District Court found [R. Vol. I, p. 143]:

"The record does not support this contention. Schnitzer's agent tried to put the vessel in at this particular wharf, but could not do so *on account of the nature of the vessel's scrap. The scrap could not be discharged in seven days, and, therefore, was not eligible for space at the particular wharf* (emphasis supplied)."

The Nictric was actually delayed $82\frac{1}{2}$ days in excess of the lay time provided under the charter (the lay days expired October 9 at 12:18, Pretrial Order, Admitted Facts X [R. Vol. I, p. 105] and discharge was completed December 31, 1961, at 0001 hours, Admitted Facts VIII [R. Vol. I, p. 105]. Subtracting from this period the delay of one week suffered by the next-most delay ridden category of cargo reported by Pacific Marine namely "ore, coal, grain and other commodities going into consignees' own installations or into clean cargo lighters," the delay caused by the nature of the cargo amounted to $75\frac{1}{2}$ days.

The evidence as to which there is no conflict whatever is that the expenses of Amtro of operating the Nictric during the period of the delay were \$1,150.00 a day [Testimony of Mr. Stewart, R. Vol. II, pp. 50-51]. The demurrage rate was \$700 a day.

Therefore, under evidence as to which there was no conflict, the extra expense to Amtro by reason of the nature of the cargo was \$450.00 a day times $75\frac{1}{2}$ days. or a total sum of \$33,975.00. The District Court erred in failing to award this sum to Amtro, and the judgment, of the District Court must be reversed on this point with directions to enter judgment in favor of Amtro against Schnitzer in that sum.

III.

The District Court Erred in Construing Clause 23 of the Time Charter Between Amtro and Owners Relating to Crew Overtime.

The single point on which Amtro is appealing from the judgment of the District Court in favor of owners against Amtro is the inclusion by the District Court in that judgment of the sum of \$1,658.41, as contended by Owners rather than the sum of \$478.47, as contended by Amtro as the amount payable by Amtro to owners under clause 23 of the time charter [Lib. Ex. 1]. The issue is one of construction of the clause. The clause is a clause in the printed form of the time charter which was modified in this particular charter by crossing out certain words and substituting others. The clause is as follows, with the words which were crossed out appearing in parentheses, and the words which were added being italicized:

“23. Vessel to work night and day, if required by Charterers, and all winches to be at Charterers’ disposal during loading and discharging; steamer to provide one winchman per hatch to work winches day and night, if required, Charterers agreeing to pay (officers, engineers, winchmen, deck hands and donkeymen for overtime work done in accordance with the working hours and rates stated in the ship’s articles) *\$350.00 per month or pro rata in lieu of all overtime.*”

The issue is whether the \$350.00 per month or pro rata is payable by charterer only during loading and discharging operations, in which case the amount payable

was stipulated to be \$478.47, or during the entire period of the charter regardless of what the vessel was doing, in which case it was stipulated that the amount payable was \$1,658.41. The District Court adopted the latter construction of the clause on the following reasoning [R. Vol. I, pp. 133-134] :

“The record discloses that the substitution was made in order to eliminate the need for mathematical calculations and record keeping. If, as argued by Amtro, the language be interpreted to mean that the overtime should apply only during periods of loading and discharge, there would have been no need for the elimination of the quoted language, nor for the substitution of the underlined language. True enough, the substituted language is subject to a charge of ambiguity. Nevertheless, when read in the light of the Captain’s testimony and of the deleted language, the intention of the parties assumes a cloak of understanding and dictates a finding that the parties intended a flat \$350.00 per month, or pro-rata for a partial month, regardless of the actual amount of overtime consumed. Otherwise, the substituted language is completely without meaning.”

The conclusion does not follow from the court’s premises, and is wrong. Under either interpretation of the clause, the necessity for record keeping with respect to the overtime actually worked and the amounts payable for such overtime which would be necessary under the printed language are eliminated. It makes little difference to the record keeping or the calculation involved whether the payment at the monthly rate is based on

the total time elapsed under the charter or the time when the vessel is loading or discharging.

Under the original printed language, it is clear that the only overtime payable by the charterer is overtime caused to owners by their making the crew available under clause 23 for night work during loading and discharging. Crew overtime during any other period is borne by the owners. Therefore, when the words requiring charterer to pay overtime worked are crossed out and the words "\$350.00 per month or pro rata in lieu of all overtime" are substituted, the overtime that the stipulated monthly payment is "in lieu of" must be only the overtime during periods when the owners may be required to comply with the clause, and not other overtime for which owners would have to pay anyway. Therefore, a \$350.00 per month payment must be applicable only during periods of loading and discharging. If the \$350.00 per month were intended to be payable continuously during the period of the charter there would be no reason to provide for it separately. The monthly charter hire would simply have been increased by that amount.

On the foregoing grounds judgment of the District Court in favor of Amtro against owners must be reversed on this point with direction to reduce the amount of the judgment by the sum of \$1,179.94.

Conclusion.

We submit that the decree of the District Court, though it should be affirmed except as to the points raised on this cross-appeal, must be reversed on those points, with directions to modify the decree as follows:

1. To add to the amount of the present decree in favor of Amtro against Schnitzer the sum of \$24,745.27 plus interest at 6% per annum from February 6, 1962 (that being the interest allowed owners against Amtro on the damages for breach of time charter);

2. To add to the present decree in favor of Amtro against Schnitzer the further sum of \$33,975.00.

3. To reduce Owners' decree against Amtro for the amounts due under the time charter in the sum of \$1,-179.94.

Respectfully submitted,

ALEX L. PARKS,
DUSENBERY, MARTIN, BEATTY,
PARKS & TEMPLETON,
ROBERT A. FLETCHER,
FLETCHER & RAUCH,

*Proctors for Cross-Appellant Amtro
Corporation, S.A.*

Certificate.

I certify that, in connection with the preparation of this brief, I have examined Rules 18 and 19 of the United States Court of Appeals for the Ninth Circuit, and that, in my opinion, the foregoing brief is in full compliance with those rules.

ROBERT A. FLETCHER

FEB 14 1967

No. 20526

United States
COURT OF APPEALS
for the Ninth Circuit

SCHNITZER STEEL PRODUCTS CO.,
a corporation,

Appellant,

v.

AMTRO CORPORATION, S.A., a Panamanian
corporation, and CIA. ESTRELLA BLANCA,
LTDA., as Owner of the SS NICTRIC,

Appellees.

v.

SCHNITZER STEEL PRODUCTS CO.,
a corporation, and

CIA. ESTRELLA BLANCA, LTDA.,
as Owner of the SS NICTRIC,

Cross-Appellees.

**BRIEF OF CROSS-APPELLEE SCHNITZER STEEL
PRODUCTS CO. ON CROSS-APPEAL**

*Upon Appeal from the United States District Court
for the District of Oregon*

HONORABLE JOHN F. KILKENNY, Judge

GUNTHER F. KRAUSE,
CARL R. NEIL,
KRAUSE, LINDSAY & NAHSTOLL,

Ninth Floor, Loyalty Building
Portland, Oregon 97204,

*Proctors for Appellant,
Schnitzer Steel Products Co.*

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WM. B. LUCK, CLERK



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**BRIEF OF CROSS-APPELLEE SCHNITZER STEEL
PRODUCTS CO. ON CROSS-APPEAL**

*Upon Appeal from the United States District Court
for the District of Oregon*

HONORABLE JOHN F. KILKENNY, Judge

STATEMENT OF THE CASE

Amtro's Statement of the Case in its brief on cross-appeal states as facts several things which are without support in the record, and makes other statements of

fact which are disputed in this cross-appeal or in Schnitzer's appeal, or both. Schnitzer therefore does not adopt Amtro's statement of the case on its cross-appeal. Schnitzer's differences with Amtro on what the record shows or does not show, however, can be more conveniently set forth in argument answering the points raised by Amtro in its brief on cross-appeal.

SUMMARY OF ARGUMENT

I

Schnitzer is not liable for the damages awarded to Owners against Amtro for breach of the time charter in failing to pay the time charter hire.

1. Amtro's claim on its cross-appeal for recovery of additional damages against Schnitzer depends in the first instance on the question of whether Schnitzer was liable for demurrage under the voyage charter terms. If Schnitzer was not liable for it, as Schnitzer asserts on its appeal, there was no breach of the voyage charter and thus no basis for Amtro claiming further sums as consequential damages for breach of contract or for tort.

2. Neither the length of the delay in discharge nor Amtro's loss of its time charter for failure to pay charter hire were reasonably foreseeable consequences when the voyage charter was entered of Schnitzer's nonpayment of demurrage.

3. The measure of damages for failure to pay a liquidated sum of money is recovery of the sum plus interest from the date payment was due.

4. There is no evidence that Schnitzer's failure to pay the demurrage was the legal cause of Amtro's unwillingness or inability to pay the time charter hire it owed to Owners.

5. Amtro failed to avoid or minimize its loss by exercising its lien on cargo to collect the demurrage.

6. There is, at the least, a substantial question of whether Schnitzer is liable for the demurrage. A party to a contract should not be required to choose between abandoning his right to litigate a questionable obligation and the risk of substantial additional damages if the disputed question is decided adversely to him in the courts.

7. Nonpayment of a questionable debt does not constitute the tort of wrongful interference with contractual relations between the promisee and a third party. There is no evidence of intent by Schnitzer to interfere with Amtro's relations under its time charter with Owners, nor any causal relationship between Schnitzer's nonpayment of demurrage and Amtro's failure or inability to pay the time charter hire to Owners.

II

The difference between the agreed demurrage rate and Amtro's expenses during the demurrage period or any portion of it is not recoverable as "extra expenses" under Clause 1 of the voyage charter party.

1. The "extra expense" clause was intended to deal with expenses attributable to turnings, which might require special handling or precautions.

2. There is no evidence that all or any part of the delay in discharge was due to the cargo being scrap, rather than logs, lumber, grain or any other cargo.

3. The demurrage clauses of a charter party are the agreed compensation for delay of the vessel in loading or discharge beyond the agreed period.

ARGUMENT

I

Schnitzer is not Liable for the Damages Awarded to Owners against Amtro for Breach of the Time Charter in Failing to Pay the Time Charter Hire.

Amtro breached its time charter (Ex. 1) of the NIC-TRIC by failing to make the monthly charter hire payments due in November and December, 1961 (R. 132). Owners therefore withdrew the vessel from the time charter upon completion of cargo discharge on December 31, 1961. The District Court awarded damages to Owners against Amtro for breach of the time charter in the amount of \$24,745.27 (R. 136).

Amtro claims that it should be allowed to recover these damages for breaching its time charter from Schnitzer, on either of two theories:

(a) As consequential damages flowing from Schnitzer's alleged breach of the charter party in failing to pay the demurrage; or

(b) As damages for Schnitzer's alleged tort of wrongful interference, in failing to pay the demurrage, with contractual relations between Amtro and Owners.

The District Court denied recovery to Amtro against Schnitzer on this matter. It found the consequential damage theory inapplicable, and did not discuss the tort theory because it was neither presented nor argued to the District Court by Amtro. The Court's opinion and findings in full on this phase of the case were as follows (R. 148):

"CONSEQUENTIAL DAMAGE

"This demand is an alternative to the claim for fraud. Amtro urges that Schnitzer's refusal to pay the balance of the freight and demurrage, when due, caused the withdrawal of its time charter, and as a result consequential damage was inevitable. To be conceded is the fact that judgment in the sum of \$24,745.27 and interest is being allowed to Owners as damages for breach of the time charter. The issue presented is whether Schnitzer is liable in whole, or in part, for this or other loss.

"After a complete analysis of the evidence before me, I do not believe that it would support a finding that either Amtro or Schnitzer contemplated the long delay which was incurred at the ports of discharge, nor could Schnitzer contemplate that its failure to pay demurrage would result in a withdrawal of the charter and consequential damages as herein fixed. As a general rule, under a charter such as this, the amount fixed as demurrage, and interest allowed thereon, fixes the amount of damages. *Globe Refining Co. v. Landa Cotton Oil Co.*, 190 U.S. 540 (1903); *Poor, Charter Parties & Ocean Bills of Lading*, Sec. 82; *Earnline S. S. Co. v. Manati Sugar Co.*, 269 F. 774 (2d Cir. 1920). This record does not support the allowance

of consequential damages to Amtro, in addition to demurrage.”

Amtro admits in its brief on cross-appeal, p. 16, that the District Court’s findings are supported by evidence and binding.

In contending that Schnitzer is liable for additional sums either as consequential damages for breach of contract or as damages for tortious interference with contractual relations, Amtro assumes that Schnitzer was in fact and in law liable in the first instance and obligated to pay the demurrage to Amtro under the terms of the voyage charter. If, as Schnitzer contends on its own appeal and briefs in support thereof, it was not liable to Amtro for the demurrage, there was no breach of the voyage charter by Schnitzer and there could be no basis for any further liability to Amtro either in contract or tort. The Court, therefore, will not reach Amtro’s cross-appeal against Schnitzer if the award of demurrage against Schnitzer is reversed on its appeal.

A. Amtro’s Breach of its Time Charter and the Damages awarded to Owners for it are not Recoverable from Schnitzer as Consequential Damages for Failure to Pay Demurrage.

It is a universal and long-accepted rule of contract law that damages for breach of contract are limited to compensation for those consequences reasonably foreseeable or within the contemplation of the parties when the contract was entered. 5 Williston, CONTRACTS (Rev. Ed. 1937) Sec. 1344. The leading American case is Justice Holmes’ opinion for the Court in *Globe Refining*

Co. v. Landa Cotton Oil Co., 190 U.S. 540, 23 S. Ct. 754, 47 L. Ed. 1171 (1902). The rule is applicable in admiralty to a breach of charter party. *Earn Line S. S. Co. v. Manati Sugar Co.*, 269 F. 774, 777 (C.C.A. 2, 1920); Poor, *CHARTER PARTIES & OCEAN BILLS OF LADING* (4th Ed. 1954) Secs. 82, 84.

The rule looks to what the parties could reasonably foresee or contemplate as harm from a breach of contract when they entered the contract, and not at some later date during its life. Justice Holmes stated this clearly in the *Globe Refining Co.* case, *supra*:

"This point of view is taken by implication in the rule that 'a person can only be held to be responsible for such consequences as may be reasonably supposed to be in the contemplation of the parties at the time of making the contract.' [citation of cases omitted] The suggestion thrown out by Bramwell, B., in *Gee v. Lancashire & Y. R. Co.* 6 Hurlst. & N. 211, 218, that perhaps notice after the contract was made and before breach would be enough, is not accepted by the later decisions. See further, *Hydraulic Engineering Co. v. McHaffie*, L.R. 4 Q.B. Div. 670, 674, 676. The consequences must be contemplated at the time of the making of the contract." (190 U.S. at 544)

The evidence clearly supports the Court's findings (R. 148) that neither Amtro nor Schnitzer contemplated, when entering the voyage charter, the extraordinary delay in discharging the cargo (Tr. 43-45, 154, 186; Ex. 79, pp. 6-8).

Nor, as the Court found (R. 148), is there any evidence that Schnitzer could reasonably have then

foreseen that failure to pay demurrage would result in withdrawal of the time charter for Amtro's failure to pay the monthly charter hire. There is no evidence that Schnitzer when entering the voyage charter had any knowledge whatever of the terms of the time charter between Owners and Amtro, the financial structure of Amtro, that the NICTRIC charter was Amtro's first or only venture, or of Amtro's actual or potential sources of revenue for paying charter hire on its time charter of the NICTRIC. Mr. Leonard Schnitzer testified that the identity of the particular vessel and its time charterer was kept secret by the charter broker, in accordance with brokers' custom, until the terms of the voyage charter were thought to have been fixed (Tr. 172-173, 178). Knowing nothing about Amtro's finances or operations, Schnitzer could hardly be expected to anticipate when the voyage charter was entered that payment of demurrage money several months later would become essential for Amtro to keep up its time charter hire payments to Owners.

A promisee's inability to perform a collateral contract because of its promisor's breach of contract is not compensable as consequential damages for the promisor's breach, either in admiralty or civil law, in the absence of the promisor's special knowledge when making his contract of the collateral contract between the promisee and another party and of the probable effect of his breach on the promisee's ability to perform the collateral contract. *Globe Refining Co. v. Landa Cotton Oil Co.*, *supra*; *Continental Grain Co. v. Armour Fertilizer Works*, 22 F. Supp. 49, 55 (S.D. N.Y.

1938); 5 Williston, *CONTRACTS*, Sec. 1355. While Schnitzer knew when signing the voyage charter that Amtro was time charterer of the vessel, there is no evidence that it had any knowledge whatever when the voyage charter was entered that there would be extensive delay in discharge or that failure to pay demurrage would bring about loss of Amtro's time charter from Owners. For all Schnitzer then knew, the entire time charter hire might have been prepaid.

Where the breach of contract is a failure to pay a liquidated sum of money, the measure of damages is interest on the sum from the time payment was due, together with recovery of the principal itself. *Loudon v. Taxing District of Shelby County*, 104 U.S. 771, 26 L. Ed. 923 (1882); 5 Williston, *CONTRACTS*, Sec. 1410. Amtro's claim here is founded simply on failure of Schnitzer to pay the demurrage money, and not on the fact that extensive demurrage was incurred due to delay in discharging. Amtro itself claims that the time charter could have been re-instated despite the long period on demurrage if Schnitzer had simply paid the demurrage monies on completion of discharge or shortly thereafter (See Amtro's Brief on Cross-Appeal, pp. 13-14). Since the voyage charter stipulated both the beginning date of the demurrage period and the rate of demurrage during the period, the amount of the demurrage monies was fixed upon completion of discharge.

The rule that interest provides the damages for breach of an obligation to pay money is more than a

rule of convenience. It requires sheer speculation in almost any such case, including this one, to say that failure of the promisee to pay a sum of money, rather than any other source of the promisee's financial difficulty, is the cause of the promisee's lack of funds to meet collateral obligations. Could Amtro have borrowed the sums necessary to meet the time-charter hire payments? Was Amtro undercapitalized from the beginning for this business? Did it use its \$100,000 capital (Tr. 52-53, 67) and revenues (at least 90 per cent of the \$65,000 NICTRIC voyage charter hire, R. 105) improvidently? Did it have other reasons than the unloading delay on this voyage and lack of demurrage monies for deciding not to pay time-charter hire and allowing withdrawal of the vessel, such as lack of cargoes for a return voyage (Tr. 60 et seq.)? There may be many reasons for or causes of a promisee's lack of funds to perform a collateral contract, and it cannot be proved in this or any other case that the promisor's failure to pay a sum due under its contract was the efficient or principal cause of the promisee's breach of the collateral contract. All that this record may show is that the demurrage monies on completion of discharge may have been more than the amount necessary for Amtro to re-instate the time charter. For all the record shows, Amtro may also have had other creditors who would have seized enough of the demurrage monies, if paid, to reduce the sum below the delinquencies under the time charter.

In short, there is every reason for adhering in this case to the well-settled rules of damages for breach of contract that compensable loss must have been rea-

sonably within the contemplation of the parties when the contract was entered, and that interest is the measure of damages for failure to pay a liquidated sum of money due under a contract. Neither the unusual delay in discharge nor loss of Amtro's time charter after non-payment of demurrage was reasonably foreseeable by the parties when the voyage charter was entered. There is no evidence that nonpayment of the demurrage, any more than any other factor contributing to Amtro's financial condition, was the legal cause of Amtro's failure or inability to pay time-charter hire.

Moreover, Amtro failed to avoid or minimize its loss by means readily available to it for collecting the demurrage monies, if they were essential to meeting its time charter obligations. The voyage charter (Ex. 2) gave Amtro a lien expressly to provide security for the payment of demurrage. Amtro could have exercised its lien on the cargo by stopping discharge until the consignees paid or gave security for the demurrage and it could have sold the cargo to collect these sums, if necessary. As shown in Schnitzer's opening brief on its appeal (p. 51 et seq.), Amtro made no efforts to do any of these things, although it had begun to threaten exercise of the lien shortly after demurrage began to accrue in October 1961 (Tr. 80-81, 192-193). Amtro's failure to use means readily available to it to collect the demurrage and thereby avoid loss of its time charter precludes it from claiming additional damages, as well as the demurrage. *New York & Cuba Mail S. S. Co. v. Lamborn*, 13 F.2d 535 (CCA 2 1926); *Continental Grain Co. v. Armour Fertilizer Works*, 22 F. Supp. 49,

55 (SD NY 1938); 4 Williston, *CONTRACTS*, Sec. 1099B, p. 3102.

Although admitting its lack of any authority in point for doing so (Br. p. 21), Amtro would have the Court create a rule that one who denies a questionable liability for payment of a sum of money must either abandon his right to litigate the question of liability in the courts and pay the disputed sum, or run the risk of suffering a penalty by way of unforeseen additional damages if he litigates the initial liability question and receives an adverse decision. Such a rule, of course, would put unjustifiable coercive power in the hands of the claimant to a disputed debt by forcing the alleged obligor to predict, at the peril of vastly increased damages, how the courts will decide disputed questions of law and fact.

The briefs of the parties on Schnitzer's appeal on the demurrage question show, at the very least, that there is a good-faith question whether Schnitzer is liable for the demurrage under the terms of the voyage charter party. It is not reasonable to assume, as Amtro does, that Schnitzer would arbitrarily and without good-faith belief in its position refuse to pay the demurrage after notice that non-payment would result not only in a suit for the principal sum and interest, but also a claim by Amtro for substantial additional damages for loss of its time charter (see Amtro's Brief, p. 14, footnote 4), as well as interest on a large amount of demurrage.

There may be cases where refusal to perform a disputed obligation is so maliciously-intended and bereft

of reason or good faith that some sort of penalty by way of increased damages is merited. This case is not one of them.

B. Non-Payment of a Questionable Debt is not a Tort.

Even more strained is Amtro's argument (Brief, p. 28 et seq.) that Schnitzer's failure to pay the demurrage constituted the tort of intentional and unjustifiable interference with Amtro's contractual relations with Owners (the time charter). This claim was not presented or argued to the District Court, and therefore was not decided by it.

It is clear that actionable interference with contractual relations arises only where the acts claimed to be wrongful were intended to induce a breach of a collateral contract between other parties. 1 Harper & James, TORTS (1956) Sec. 6.6, pp. 492-493. Amtro's brief seems to concede this at p. 34. There is no evidence in this case that Schnitzer's refusal to pay the demurrage here was based on anything other than its belief that it was not liable for it, under the terms of the voyage charter party.

The Knickerbocker Ice Co. cases¹ cited by Amtro (Brief, p. 33 et seq.) involved the defendant's refusal to honor supply contracts, with the express intention of inducing the promisee to cease contractual relations with a third party, in order to force the third party to buy from the defendant at higher prices.

¹ *Knickerbocker Ice Co. v. Gardiner Dairy Co.*, 107 Md. 556, 69 A. 405 (1908); *Sumwalt Ice Co. v. Knickerbocker Ice Co.*, 114 Md. 403, 80 A. 48 (1911).

Schnitzer had the right and privilege of litigating in court whether it was liable for the demurrage, particularly when this suit had been commenced against it on December 14, 1961 (R. 1), before the discharge of cargo was completed on December 31, 1961, and before Amtro sent, on December 26 and January 2, 1962, its notices that payment of demurrage monies was necessary for it to meet its time-charter hire obligations (see Amtro's Brief, p. 14 footnote 4). A party cannot reasonably be charged with a tort for litigating in the courts whether it is liable for a sum of money claimed by another. Amtro has produced no authority even remotely supporting its contention to the contrary.

The weakness of Amtro's argument is apparent at p. 39 of its Brief:

"Perhaps even in the face of the known damage to the other party, a party to a contract should be privileged to refuse payment in order to assert what it believes in good faith to be a defense to payment. Even here, however, it could be argued with great force that if a party should choose to rely on such a defense in the face of known damage to the other party, the party so relying should be required to do so at its peril to the extent that, if the court subsequently holds the defense to be groundless, the party should be required to pay the compensatory damages."

Amtro's argument would have the Court hold that a tort, as well as a breach of contract, may be committed if one fails to perform a contractual obligation to pay a sum of money in the belief that he is not liable for it

and litigates the matter in court, but suffers an adverse decision on the question of contractual liability. If the court decides adversely to him, his earlier action in failing to pay money may be held to have been a tort; if the decision is in his favor, his earlier action was neither breach of contract nor tort. Surely the existence of a tort cannot depend on accurate prediction of how a court will decide disputed questions of law and fact in the interpretation and application of contractual provisions.

The *Blumenthal*² and *Poznan*³ cases relied on by Amtro (Brief, p. 35 et seq.), both involve non-performance of a contract to ship or carry goods of a third party, with resulting loss or damage to the third party. The analogy to this case would exist only if Owners here were suing Schnitzer for some harm they sustained because of Schnitzer's failure to pay the demurrage to Amtro. The tort in those cases was not a wrong committed against one in Amtro's position as the other party to the contract. Owners do not and could not assert such a claim, for reasons already mentioned: there is no evidence that Schnitzer's non-payment of demurrage was the cause of Amtro's financial inability to pay NICTRIC time-charter hire to Owners, rather than any of many other factors contributing to Amtro's financial condition or its decision not to pay the time-charter hire. Schnitzer, moreover, had the right and privilege of litigating the question of its liability for the demur-

² *Sidney Blumenthal & Co. v. U. S.*, 30 F.2d 247 (C.C.A. 2, 1929), cert. den. 279 U.S. 847.

³ *The Poznan*, 276 F. 418 (S.D.N.Y. 1921).

rage in the suit commenced by Owners against Amtro and against Schnitzer as garnishee.

II

The Difference between the Agreed Demurrage Rate and Amtro's Expenses during all or part of the Demurrage Period is not Recoverable under Clause 1 of the Voyage Charter Party.

Amtro claims that it should have been awarded \$33,975 over and above the demurrage as "extra expenses incurred by reason of nature of cargo" within the meaning of Clause 1 of the voyage charter party (Ex. 2). It claims that any cargo other than scrap would have been discharged at least 75½ days before the discharge of the NICTRIC cargo was completed, and that it incurred each day during this period expenses for operation of the vessel of \$450 over and above the agreed demurrage rate of \$700 per day (Amtro's Brief, p. 46).

The relevant part of Clause 1 in context provides:

"That the said vessel shall proceed to Vancouver, B. C. and/or Portland, Oregon, Charterers option in or out of geographical rotation or so near thereto as she may safely get and lie always afloat, and there load a full and complete cargo under deck of SCRAP AND/OR MOTOR BLOCKS AND/OR SCRAP RAILS AND/OR NON-FERROUS SCRAP AND/OR MAXIMUM 1500 TONS TURNINGS. TURNINGS TO BE LOADED IN ACCORDANCE WITH U. S. COAST GUARD AND NATIONAL CARGO BUREAU REGULATIONS AND UNDER THE SUPERVI-

SION OF A METALLURGICAL EXPERT. ANY EXTRA EXPENSES INCURRED BY REASON OF NATURE OF CARGO AND OF METALLURGICAL EXPERT TO BE FOR CHARTERERS' ACCOUNT."

The "extra expenses" referred to here are clearly any extra expenses of loading, stowing, discharging or carrying for cargo of such a nature as to require unusual handling. It clearly had reference to any possible unusual expense in shipping a quantity of turnings in the cargo, and not to scrap in general or to general delay in discharge. Carriage of the turnings was a subject of negotiation between the charter broker and Amtro in fixing the terms of the voyage charter party, and the "extra expense" clause was put in to cover any unusual expenses in handling them (Tr. 150-151, 180-182). Mr. Stewart of Amtro agreed with this, but testified that the language was put in also to cover any delay in getting the entire cargo discharged (Tr. 44). The District Court found against his testimony (R. 145-146) and adopted that of Mr. Bettinger, an employee of the charter broker which negotiated the voyage charter as to both parties (Tr. 150-151).

The District Court's opinion and findings in their entirety on this issue were as follows (R. 145-146):

"EXTRA EXPENSES

"Clause 1 of the voyage charter provides, among other things: 'Any extra expenses incurred by reason of nature of cargo and of metallurgical expert to be for charterer's account . . .' Amtro points to

this language in support of its claim for extra expenses incurred while the NICTRIC was delayed in Japan. While the record discloses that a scrap cargo, such as was carried by the NICTRIC was not favored in the discharging scheme in Japan, it does not support a finding that the total delay, or any specific part thereof, was due to the nature of the cargo. Furthermore, it would require the imagination of a leprechaun to extend this language to cover a situation where a ship carrying scrap was compelled to wait longer to obtain a berth than ships carrying other kinds of cargo. Obviously, the 'extra expenses' mentioned in this clause refer to those expenses, if any, directly incurred in loading, transporting or discharging the scrap. Likewise, the fundamental purpose of demurrage is to make an adequate allowance or compensation for the delay or detention of the vessel. *THE CONQUEROR*, 166 U.S. 110 (1897); *Continental Grain Co. v. Armour Fertilizer Works*, 22 F. Supp. 49, 54 (S.D. N.Y. 1938); *THE APOLLON*, 22 U.S. 361, 376 (1824); *W. R. Grace & Co. v. Hansen*, 273 F. 486, 496 (9th Cir. 1921). The claim for alleged extra expenses is denied."

Amtro does not claim that it incurred any extra expense in shipping or handling turnings or other unusual cargo. Instead, it claims that its expenses of operating the vessel are recoverable, to the extent they exceeded demurrage, for that portion of the demurrage period extending beyond the period which it claims that a cargo other than scrap would have been delayed.

In addition to the fact that Clause 1 was intended to deal only with any extra expenses incurred in

handling turnings or other peculiar or hazardous cargo, there are other obvious reasons why Amtro's claim fails.

First, as the Court found, there is no substantial evidence that all or any part of the delay was due to the fact that the cargo was scrap. Ex. F-23, relied on by Amtro (Brief, p. 44), was a report dated September 15, 1961, assembled from data collected earlier and did not purport to deal with conditions in the NICTRIC demurrage period, which began October 9, 1961 (R. 105). It was inadmissible hearsay, in any event (See Schnitzer's opening brief on its appeal, pp. 66-67). Neither the report nor any other evidence cited by Amtro would enable a court to find how much less, if any, delay would have been experienced after October 9, 1961, if the NICTRIC, a tramp vessel, had carried logs, lumber, grain or any other cargo. The Court found that Harumi Wharf could not be used because discharge could not occur in seven days, not because the cargo was scrap (R. 143, cf. Amtro's Brief, p. 45). Harumi was a special discharge berth for scrap cargo (Ex. 44H, p. 187-2).

Secondly, the demurrage clauses of the voyage charter were designed and intended by the parties to compensate Amtro for delay beyond the agreed laydays. The parties after negotiations agreed upon a rate of \$700 per day for demurrage (Ex. 2, Clauses 7, 18). Schnitzer wanted a rate of only \$600 per day, while Amtro originally demanded \$1100 per day (Tr. 83). It is common for the agreed demurrage rate to be less than the actual expenses of operating the vessel (Ex.

79, p. 9). If Amtro wished to charter the vessel only if a demurrage rate equal to its operating costs was agreed on, it was free to do so and to refuse to enter the charter on any other terms. Moreover, Amtro demanded but did not get a clause in the voyage charter party guaranteeing that the laydays would not be exceeded (Tr. 83). In short, delay, as Amtro knew, is always possible in ocean carriage, and ^{demurrage} was intended to be the agreed compensation for delay in excess of the agreed period for loading and discharging.

The cases cited in the District Court's opinion, *supra*, p. 18 (R. 146), are among numerous examples of judicial recognition that demurrage clauses are intended by the parties to be the agreed compensation for expenses and loss of profits incurred by the vessel operator in delay beyond the agreed time for loading and discharging. See also *Earn Line S. S. Co. v. Manati Sugar Co.*, 269 F. 774, 776 (C.C.A. 2 1920); *Steger v. Orth*, 258 F. 619, 623-624 (C.C.A. 2 1919); 4 Williston, *CONTRACTS*, Sec. 1099B, p. 3102.

CONCLUSION

The District Court was plainly correct in denying Amtro's claims against Schnitzer for additional damages and "extra expenses." There is plainly no basis in the circumstances shown by the record or in the law for regarding the damages awarded to Owners against Amtro for breach of time charter as consequential damages to Amtro from Schnitzer's failure to pay demurrage money, when Schnitzer's liability is at least question-

able. Even less tenable is Amtro's claim that Schnit-
 zer's conduct constituted intentional and unjustifiable
 interference with Amtro's contractual relations in the
 time charter with Owners. The "extra expense" clause
 has no relation to delay in discharge of the cargo, the
 demurrage clauses providing the agreed compensation
 for delay in discharge.

Those portions of the District Court's decree chal-
 lenged by Amtro's cross-appeal should therefore be af-
 firmed.

Respectfully submitted,

GUNTHER F. KRAUSE

CARL R. NEIL

KRAUSE, LINDSAY & NAHSTOLL

Proctors for Schnitzer Steel
 Products Co.

CERTIFICATE OF COUNSEL

I certify that, in connection with the preparation of
 this brief, I have examined Rules 18 and 19 of the
 United States Court of Appeals for the Ninth Circuit
 and that, in my opinion, the foregoing brief is in full
 compliance with those rules.

CARL R. NEIL

Of Proctors for Schnitzer Steel
 Products Co.



FEB 14 1967
No. 20526
IN THE

United States Court of Appeals

FOR THE NINTH CIRCUIT

SCHNITZER STEEL PRODUCTS CO., a corporation,
Appellant,
vs.

CIA. ESTRELLA BLANCA, LTD., as owner of the S.S.
NICTRIC, and AMTRO CORPORATION, S.A.,
Appellees.

AMTRO CORPORATION, S.A.,
Cross-Appellant,

SCHNITZER STEEL PRODUCTS CO., a corporation, and
CIA. ESTRELLA BLANCA, LTD.,
Cross-Appellees.

Reply Brief for Cross-Appellant Amtro Corporation,
S.A. on Cross-Appeal.

ALEX L. PARKS,
DUSENBERY, MARTIN, BEATTY, PARKS
& TEMPLETON,

ROBERT A. FLETCHER,
FLETCHER & RAUCH,

4050 Wilshire Boulevard,
Los Angeles, Calif. 90005,

*Proctors for Cross Appellant Amtro
Corporation, S.A.*

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Reply Brief for Cross-Appellant Amtro Corporation,
S.A. on Cross-Appeal.

Most of the points urged in Schnitzer's brief on Cross-Appeal are fully answered in Amtro's Opening Brief, and will not be covered again here. The following can be added:

I.

DAMAGES FOR BREACH OF
CONTRACT AND TORT.

A. Schnitzer Asserts That the Damages Sought
by Amtro Amount to a "Penalty" Against
Schnitzer for the Assertion of a "Good Faith"
Defense to Liability for the Demurrage.
Schnitzer Is Wrong on Both Counts:

1. The damages sought by Amtro are not, as Schnitzer asserts (Br. p. 12), a "penalty." They are only the actual damages suffered by Amtro as the direct result of Schnitzer's failure to discharge the vessel within the time agreed in the charter and Schnitzer's subsequent failure to pay the demurrage. The admitted facts demonstrating this are outlined on pages 12-14 of Amtro's Opening Brief. Schnitzer (Br. p. 10) advances some speculations in an attempt to cast doubt on the causal connection between Schnitzer's acts and Amtro's damages. There is no support whatever in the record for any of the speculations advanced. Mr. Stewart, Amtro's managing officer, testified at the trial, and Schnitzer could have inquired into these matters by cross-examination had it cared to. The Pre-Trial Order gave ample notice of Amtro's contentions on the material points [R. Vol. I, p. 111, lines 28-29; p. 112, lines 2-5].

Schnitzer complains (Br. p. 12) of having been required to decide at its peril whether to pay what it now calls the "disputed" obligation, or to contest it and bear the damages to Amtro caused thereby. The complaint is a strange one. Throughout the various relationships governed by the law, a party must always act at its peril to that extent. There was nothing "unforeseen"

about these damages at the time Schnitzer made its decision not to pay. At that time, upon the completion of discharge of the Nictric, Schnitzer had specific notice from Amtro of the damages which would be caused to Amtro by Schnitzer's refusal of payment.

What Schnitzer is really claiming is a vested interest in the invariable application of the common rule limiting damages to interest on the money. Schnitzer wants always to be able to say, "Since the damages, if I refuse to fulfill my contract, are limited to interest in any event, and since I can use the money more profitably than the interest rate, why should I pay?" Any mechanical rule permitting a party to calculate its advantages in this way, no matter what the consequences to the other party, is manifestly unjust. None of the cases which we have been able to find limiting damages to interest, including *Loudon v. Taxing District of Shelby County*, 104 U.S. 771, 26 L. Ed. 923 (1882), cited by Schnitzer, involve situations where the party refusing to pay did so in the face of notice of the damages which would be caused thereby to the other party.

By the same token, none of those cases involve situations where the damages flowed both from the breach of an obligation to pay money and from the breach of another contractual obligation, such as the obligation of Schnitzer under the voyage charter to discharge the vessel on time. While it is true, as Schnitzer points out (Br. p. 9) that these damages would have been avoided if Schnitzer had paid the demurrage, it is equally true that they would have been avoided if Schnitzer had discharged the vessel within the time contracted.

2. Throughout its brief, Schnitzer asserts that there was a "good faith" question whether it was liable for

the demurrage. Schnitzer further argues (Br. p. 12), "It is not reasonable to assume as Amtro does that Schnitzer would arbitrarily and without good faith belief in its position refuse to pay the demurrage after notice . . .". This is no "assumption" on Amtro's part. It is what the evidence indubitably shows. The "question" raised by Schnitzer at the trial and on this appeal concerning its liability for the demurrage is based on an interpretation of the charter exactly opposite to the interpretation Schnitzer was adopting at the time it faced the alternative, and decided not to pay. The District Court so found [R. Vol. I, pp. 140-141]. The evidence compelling that finding is set forth and analyzed in owners' brief, pages 14-19, and in Amtro's answering brief on Schnitzer's appeal, pages 11-14. Schnitzer was not, as its brief asserts (Br. p. 14), "one who fails to perform a contractual obligation to pay a sum of money in the belief that he is not liable for it."

B. Amtro Did Not Fail to Act Reasonably to Mitigate Its Damages.

Schnitzer claims that Amtro could have collected the demurrage by exercising a lien on the cargo, and could have thereby avoided loss of the time charter (Br. p. 11). Schnitzer suggests that Amtro could have exercised its lien on the cargo by stopping discharge until the consignees paid or gave security for the demurrage, or could have sold the cargo to collect these sums. But the District Court specifically found that if Amtro had done this, "the ship risked not only the possibility but also the probability of being moved by the harbor authorities and sent to anchor outside to await another turn at discharge" [R. Vol. I, p. 142]. The evidence supporting this finding is thoroughly discussed in

Owners' brief. Obviously the wait for another turn to discharge would have produced additional demurrage far in excess of the amounts Amtro is now claiming as damages.

Moreover, the time charter [Lib. Ex. I] clauses 4 and 5, required payment of the charter hire in cash in U. S. currency. The voyage charter [Lib. Ex. II] clauses 18 and 1, likewise required Schnitzer to pay the demurrage and freight in U. S. currency. Schnitzer does not attempt to explain how Amtro could have obtained U. S. currency with which to pay the time charter hire from the Japanese consignees or by liening the cargo in Japan.

C. Amtro Is Entitled to These Damages for Breach of Contract.

For the proposition that notice of consequential damage given after the contract was made and before breach is not enough to charge the breaching party with liability for the consequential damages, Schnitzer cites only the remark which it quotes (Br. p. 7) by Justice Holmes in *Globe Refining Co. v. Landa Cotton Oil Co.*, 190 U.S. 540, 23 S. Ct. 754, 47 L. Ed. 1171 (1902). This remark was not a holding of the court, or a considered opinion of Justice Holmes on a question which made any difference to the issues presented for decision. There was no allegation in that case (as there is evidence in the present one) that the defendant had received notice of the consequential damages at a time when the defendant was able to perform, and simply chose not to perform.

The only holding we have been able to find on the contract law question presented in this case (and

Schnitzer has apparently been able to find nothing to the contrary) is the decision of the Supreme Court of Texas in

Bourland v. Choctaw, O. & G. Ry. Co., 99 Tex. 407, 90 S.W. 483 (Supreme Court of Texas, 1906),

discussed and quoted in Amtro's Opening Brief pages 21-25. We submit that the reasoning of this case is correct and should be followed.

D. The Damages Are Also Recoverable Against Schnitzer in Tort.

It is not true, as Schnitzer seems to be asserting in its brief, that actionable interference with contractual relations arises only where the actor induces a breach of the collateral contract in order to garner its advantages to himself. The actor may be equally liable in tort where he has interfered with the collateral contract in pursuit of his own unrelated ends, but with knowledge that his conduct will prevent performance of the collateral contract. It is not a necessary element of the tort that the tort-feasor hope to profit by taking over the benefits of the collateral contract. The conduct is equally tortious where the tort-feasor does what he does in order to benefit in some other way, unless the objective sought by the tort-feasor and the means used are privileged. This is the holding of the two admiralty cases on the tort,

Sidney Blumenthal & Co. v. United States, 30 F. 2d 247 (2 Cir. 1929), cert. den. 279 U.S. 847, 73 L. Ed. 991, 49 S. Ct. 345;

The Poznan, 276 Fed. 418, 433 (S.D. N.Y. 1921, L. Hand, D.J.)

the facts and holding of which are set forth in Amtro's opening brief, pages 35-38, and of

Keene Lumber Co. v. Leventhal, 165 F. 2d 815
(1 Cir. 1948)

discussed on page 38 of Amtro's Opening Brief. That is also the view of the textwriters

Prosser, Torts, 3rd Ed. page 960;

Harper and James, Law of Torts (1956).
Volume I, page 499.

See also

Restatement of Torts, §766, comment d.

It is not true, as Schnitzer contends, that the claim for tortious interference with the performance of the time charter is one which could only be asserted by Owners in this case. The tort is actionable by either party to the contract interfered with.

Harper and James: Law of Torts (1956), Volume I, page 499.

Schnitzer's citation (Br. p. 15) of the *Blumenthal* case as supporting its contention is incorrect. In the *Blumenthal* case, the facts in which are discussed at length in Amtro's Opening Brief, pages 35-36, the U. S. Fleet Corporation was held liable to the cargo owners because the managing agents for the vessel transshipped the cargo on another vessel in violation of the terms of the bill of lading issued by U. S. Fleet Corporation to cargo. The U. S. Fleet Corporation was thus liable to cargo because the performance of its contract with cargo had been prevented by the managing agents. U. S. Fleet Corporation impleaded the managing agents for indemnity, seeking to recover from the managing agents the amount by which the U. S. Fleet Corporation had been

held liable in damages to the cargo owners. The U. S. Fleet Corporation was held entitled to recover these amounts from the managing agents for their tortious interference with the performance by the U. S. Fleet Corporation of its contract with cargo. The position of the U. S. Fleet Corporation in that case was exactly analogous to Amtro's position in this case, and that decision exactly supports Amtro's recovery against Schnitzer here.

Schnitzer's tort liability to Amtro thus depends solely on the question whether Schnitzer was privileged to do what it did. Schnitzer asserts in its brief that it refused payment in the "belief" that it was not liable for the demurrage and, in effect, claims a privilege on that ground. Whatever Schnitzer may believe now, the record contradicts any such belief on Schnitzer's part at the time, just before and immediately following discharge of the *Nictric*, when Schnitzer refused to pay Amtro. Schnitzer's present argument that it is not liable for the demurrage under the voyage charter is based entirely upon the contention that the charter required Amtro to look first to its lien upon cargo for the collection of the demurrage, that Schnitzer is liable only if it was impossible to exercise the lien, and that the lien could have been exercised. The position being taken by Schnitzer at the time Amtro demanded payment and pointed out to Schnitzer the consequences of non-payment, was exactly the reverse, namely that *Amtro had no lien*. This was the finding of the District Court [R. Vol. I, p. 141, lines 5-9]:

"Subsequently Schnitzer's counsel took the position that in fact there was no lien on cargo for the demurrage. Schnitzer relied on this construction of the contract from about November 17 until after the cargo had been discharged on December 31."

The evidence compelling that finding has been pointed out in Amtro's and owners' prior briefs.

Moreover, Schnitzer could have had a good faith belief *at that time* in the validity of its present defense to liability for the demurrage only if it had had *at that time* some information that a lien could be exercised in Japan. The uncontradicted evidence (discussed in owners' brief, pages 14-19 and in Amtro's answering brief on Schnitzer's appeal, page 13) shows that Schnitzer was advised by Amtro on December 12, 1961, and by Owners on December 14, 1961, that they each believed that it was impossible to exercise the lien in Japan. If Schnitzer had had any information to the contrary at that time, or if Schnitzer had believed at that time, as it now contends, that the exercise of the lien on the cargo in Japan would have forced the consignees and not Schnitzer to pay the demurrage, good faith and Schnitzer's own interests would have compelled Schnitzer to advise Amtro and Owners immediately of the methods by which Schnitzer believed that the lien could be exercised, and to withdraw immediately its threat of December 6 [Lib. Ex. 34] to hold owners liable in damages if they attempted to exercise a lien. Schnitzer did neither. Schnitzer kept entirely silent for fifteen days, until 2½ hours before the completion of the Nictric discharge, and then sent Amtro an unexplained denial of liability. Schnitzer did not advise Amtro or owners of its present contention that there was a lien, or of any of the methods by which it now contends a lien could have been exercised, until nearly a year later.

While the charter was in effect and the Nictric was in Japan, Schnitzer either had no belief at all in the validity of its present alleged defenses, or Schnitzer de-

liberately set out to trap Amtro. On either explanation, Schnitzer committed a tort against Amtro.

II.

EXTRA EXPENSES.

If, as Schnitzer contends, the “extra expenses” referred to in clause 1 were intended to be limited to “extra expenses of loading, stowing, discharging or carrying for cargo of such a nature as to require unusual handling, or to possible unusual expenses in shipping a quantity of turnings in the cargo,” it would have been easy for the parties to say so in the charter. The language contains no such limitations. The clause provides that “any [not just some as Schnitzer would have it] extra expenses incurred *by reason of nature of cargo* [not in the handling of cargo, or in shipping turnings, as Schnitzer would have it]” are to be for Schnitzer’s account.

Any ambiguity must be resolved against Schnitzer since, as the District Court found, the language of the charter was Schnitzer’s [R. Vol. I, p. 140]. Mr. Bettinger of Sea Charter Co. did not, as Schnitzer contends “negotiate the voyage charter as to both parties.” Under the evidence which is set out in owners’ brief, pages 10-12, Sea Charter was Schnitzer’s broker. A broker is ordinarily the agent of one or the other of the parties, and can act as the agent of both only in special circumstances.

12 Am. Jur. 2d Brokers §1, page 272, §30, page 295, §67, page 821.

That Sea Charter was Schnitzer’s broker was stated by Dr. Leonard Schnitzer in his testimony [R. Vol. II, p. 210, line 24, to p. 211, line 1].

"All negotiations for the completion of that charter were handled *by us* through Sea Charter, *our* broker. (Italics supplied)".

How Sea Charter came to call itself a broker in this transaction at all was explained by Dr. Leonard Schnitzer as follows [R. Vol. II, p. 174, line 2, to p. 175, line 7]:

"They had been acting as my agent in Portland for handling vessels that I chartered through other ship brokers, because they were ships' agents here in Portland, and I gave them business husbanding vessels, bringing people in, taking care of customs, and that sort of problem that a ship agent normally does. And during these particular negotiations I had conversations with Captain Jensen, and particularly Bettinger also. They asked if they could act as broker for us. As broker there is more commission than there is in just husbanding a vessel. So he asked if he could participate in this type of business with us, and I said, 'Yes. If you ever get a vessel, let me know.'"

The evidence showing the part of the delay that was due to the nature of the cargo, and the amount of the extra expenses, has been reviewed in Amtro's Opening Brief on the Cross-Appeal, and will not be repeated here. One thing should be pointed out. Schnitzer asserts (Br. p. 19), that "The court found that Harumi Wharf could not be used because discharge could not occur in seven days, not because the cargo was scrap." This misstates the finding of the District Court. What the District Court found was that

"Schnitzer's agent tried to put the vessel in at this particular wharf, but could not do so on account of

the nature of the vessel's scrap. The scrap could not be discharged in seven days, and therefore was not eligible for space at the particular wharf." [R. Vol. I, p. 143].

The evidence on which the District Court undoubtedly relied for this finding showed that the particular nature of the scrap placed by Schnitzer aboard the *Nictric*, in that it consisted of a mixture of varied types difficult to discharge, made it impossible to discharge the scrap within the seven days referred to. This was the testimony of Schnitzer's own witness, Mr. Koizumii, of Pacmarine, Schnitzer's agent [Ex. 44H, p. 187-26, line 19, to p. 187-27, line 2]. This was also the statement of Schnitzer's admitted employee, Mr. Morgulis, as shown by Exhibit B11, page 1, the admissibility of which is pointed out on page 31 of Owners' Brief. The extra expense for which Amtro seeks to recover was thus incurred not only by reason of the fact that the cargo was scrap, but by reason of the particular nature of this particular scrap cargo, as compared with other scrap cargos.

It is true, as Schnitzer points out (Br. pp. 19-20) that the demurrage rate was the subject of negotiation and was agreed at a rate below that necessary to cover the actual expenses of operating the vessel. Obviously part of the bargain which led Amtro to accept this low demurrage rate *applicable to delay generally* was the additional provision in clause 1 obligating Schnitzer to pay "any" extra expenses incurred by reason of nature of cargo, without limitation, thereby obligating Schnitzer to pay the extra expenses over and above the demurrage rate in the event that the vessel was delayed

from causes particularly attributable to the nature of the cargo placed on board the vessel by Schnitzer.

Demurrage provisions in a charter do not necessarily exclude other obligations of the parties on the same subject matter, where one of the parties has assumed an additional obligation in another clause. For example, in the

Ala., 1926 A.M.C. 1404 (S.D. N.Y. 1926)

a demurrage clause providing a certain number of lay days for loading was held not to detract from another provision in the charter stating that owners guaranteed to sail the vessel on or before a particular date.

III.

CLAUSE 23 OF THE TIME CHARTER RELATING TO CREW OVERTIME.

The District Court obviously relied exclusively on the testimony of Captain Cassimatis set forth in owners' brief (pp. 39-42) as its basis for interpreting the clause as it did. The District Court was in error in giving such weight to what Captain Cassimatis said. Captain Cassimatis never participated in negotiation of the time charter. Owners introduced no evidence whatever that his understanding of the clause was ever communicated to Amtro. He was the manager for the owners, and his testimony is entirely self-serving. It should not have been allowed to prevail over the only logical analysis of the clause within its four corners, which is the analysis set out in Amtro's Opening Brief.

CONCLUSION.

It is accordingly respectfully submitted that, while the District Court should be affirmed on the issue of Schnitzer's liability for freight and demurrage, it should be reversed on all of the points raised by Amtro's Cross-Appeal, with directions to modify its decree accordingly.

Respectfully submitted,

ALEX L. PARKS,

DUSENBERY, MARTIN, BEATTY, PARKS
& TEMPLETON,

ROBERT A. FLETCHER,

FLETCHER & RAUCH,

*Proctors for Cross-Appellant Amtro Cor-
poration, S.A.*

Certificate.

I certify that, in connection with the preparation of this brief, I have examined Rules 18 and 19 of the United States Court of Appeals for the Ninth Circuit, and that, in my opinion, the foregoing brief is in full compliance with those rules.

BERNARD E. O'CONNOR, JR.

No. 20537

FEB 14 1967

In the

United States Court of Appeals

For the Ninth Circuit

ALBERT J. WILD and AIR CONDITIONING
SUPPLY CO., INC.

Appellants,

vs.

UNITED STATES OF AMERICA, BENNETT Y.
BREWER, and VALLEY NATIONAL BANK,

Appellees.

Brief of Appellants

W. LEE McLANE

and

BROWN, VLASSIS & BAIN

222 North Central Ave.

Phoenix, Arizona

Attorneys for Appellants,

JACK E. BROWN

W. LEE McLANE

ARTHUR P. ALLSWORTH

Of Counsel

FILED

FEB 14 1968

WM. B. LUCK, CLERK

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UNITED STATES OF AMERICA, BENNETT Y.
BREWER, and VALLEY NATIONAL BANK,

Appellees.

Brief of Appellants

JURISDICTIONAL STATEMENT

The proceedings below were commenced by the filing of a "petition" by the United States and Bennett Y. Brewer, Special Agent (hereinafter referred to as "appellees"), purportedly under the jurisdictional grant of Section 7604(a) of the Internal Revenue Code of 1954, 26 U.S.C. § 7604(a) (1958 ed.), seeking to enforce an International Revenue summons issued by Brewer to the Valley National Bank for delivery of "[l]oan records and credit records pertaining to loans made" to appellants, including "financial statements", purportedly under the authority of Section 7602

of the Internal Revenue Code of 1954. (R. I-1.)* An order to show cause was obtained directing the Bank to show cause why it should not be compelled to obey the summons. (R. I-8.) Thereupon, appellants intervened in the proceeding (R. I-36), a response by the Bank (R. I-25) and an answer by appellants (R. I-33.) were filed and a hearing was held on said order to show cause. An order granting the petition and setting forth the opinion of the District Court was thereafter filed (R. I-88), from which appellants appealed. The jurisdiction of this Court is based on 28 U.S.C. § 1291. The Bank not having perfected an appeal, the Record herein shows the Bank as a nominal appellee.

STATEMENT OF THE CASE

The petition below alleged that Brewer had been conducting an investigation of the income tax returns of appellants "for the purpose of ascertaining the correctness of the income tax returns" filed by intervenors for the years 1960 to 1962 (paragraph IV, R. I-1) and that the Bank had certain records "which would have a direct relation to the correctness of the income tax returns" (paragraph V, R. I-2). An affidavit by Brewer submitted in support of the petition at the time of its filing alleged that he was conducting the investigation referred to as "a Special Agent of the Intelligence Division, Internal Revenue Service" and that, based upon his investigation, "he has determined that it is necessary to obtain certain financial records belonging to the Valley National Bank, in order to ascer-

*The transcript of record in this case is in two volumes, Volume I being the court file and Volume II the transcript of testimony at the hearing before the District Court. For simplicity, citations to the record ("R.") will be to the appropriate volume by Roman numerals ("I" or "II") and to the appropriate page of the volume cited by Arabic numerals.

tain the correctness of the said returns." (R. I-4.) The documents sought by Brewer were, as noted, certain "[l]oan records and credit records pertaining to loans made" to appellants, including "financial statements". (R. I-6.) The response of the Bank and the answer of appellants denied the allegations referred to without qualification and appellants' answer further averred that Brewer's investigation pertained solely to enforcement of criminal statutes and was for the purpose of prosecuting or preparing to prosecute a criminal case against appellants for an alleged violation of the criminal income tax laws. (See the Record I-25 *et seq.* and 33 *et seq.*, particularly page 33a*.) The Bank's response also affirmatively alleged that certain of the documents sought by Brewer were "totally immaterial" to his alleged investigation. (R. I-27.)

The two allegations of the petition referred to having been particularly placed in issue (with specific attention called thereto in the opening statements prior to the taking of testimony, with special reference to Treas. Reg. 1118.6 describing the function of the Intelligence Division (see R. II-23-40)), petitioners elected to offer *no* testimony concerning the allegation in the petition that Brewer's investigation was "for the purpose of ascertaining the correctness" of appellants' returns (Brewer's entire testimony is encompassed in R. II-47-53)† and, as to the appropriate-

*The Record fails to number the page following page 33, which is therefore referred to herein as page 33a.

†The only testimony which pertained to Brewer's function is his preliminary testimony that his function as a "Special Agent of the Intelligence Division" was "[t]o investigate alleged frauds against the Revenue" and (by affirmative responses to leading statements of petitioners' counsel) that he had been assigned to investigate the tax liability of appellants and had, during the course of his investigation, issued the summons sought to be enforced.

Such testimony, of course, was entirely consistent with appellants' position that Brewer's investigation was *not* "for the purpose

ness of the summons, to offer only the testimony of Brewer that he had noticed a discrepancy between the liability control sheet of the Bank showing six or seven loans to Air Conditioning Supply Co. totaling approximately \$75,000 and the books of Air Conditioning Supply Co. totaling \$6,000 (R. II-50-53).

Preliminary to the hearing above referred to, appellants also objected to the conduct of the proceeding instituted by petition and order to show cause rather than by the filing of a complaint in accordance with the Federal Rules of Civil Procedure. (R. II-40-42.)

THE QUESTIONS PRESENTED

The questions presented on this appeal, then, are as follows:

- (1) Whether the evidence presented in support of the petition was sufficient to warrant enforcement of the summons issued by Brewer, referring specifically to
 - (a) The allegation of the petition that Brewer's investigation was "for the purpose of ascertaining the correctness" of appellants' income tax returns;
 - (b) The allegation of the petition that the records sought "would have a direct relation to the correctness" of appellants' returns; and
 - (c) The inferential allegation in Brewer's affidavit that the records sought were required by him "in order to ascertain the correctness" of appellants' returns?

of ascertaining the correctness of appellants' returns" but was instead related solely to the enforcement of criminal income tax statutes (the existence of some "tax liability" regardless of the amount, being an element of criminal income tax liability).

(2) If so, whether enforcement of the summons in the circumstances presented would involve a violation of the Fifth and Fourth Amendments to the Constitution of the United States?

(3) Whether the "petition" below should have been dismissed in any event as procedurally improper under the Federal Rules?

SPECIFICATION OF ERRORS

A specification of the errors of the District Court relied upon in connection with this appeal is as follows:

(1) The District Court erred in holding, inferentially, that appellees had proven sufficiently that Brewer's investigation was "for the purpose of ascertaining the correctness" of appellants' income tax returns and in failing to find that, to the contrary, such investigation was not for such purpose but instead was solely to assist appellees with respect to the enforcement of criminal statutes.

(a) The District Court erred in holding that, since there was a possibility that a criminal prosecution might not ensue, appellants' investigatory purpose was proper.

(2) The District Court erred in holding, inferentially, that appellees had proven sufficiently that the records sought "would have a direct relation to the correctness" of appellants' income tax returns and in failing to find that, to the contrary, such records would not have any relationship to the correctness of appellants' income tax returns.

(a) The District Court erred in holding that, since the records sought "relate to financial transactions of the taxpayer being investigated," they thereby

“would have a direct relation to the correctness” of appellants’ income tax returns. (R. I-89.)

(3) The District Court erred in holding, inferentially, that appellees had proven sufficiently that the records sought were required in order to ascertain the correctness of appellants’ returns and in failing to find that, to the contrary, such records were not so required because the information sought therefrom was already in Brewer’s possession.

(a) The District Court erred in holding that “there has been no evidence presented indicating that all the records and information sought belonging to the Bank are ‘already within the Commissioner’s possession’ ” (R. I-89).

(b) The District Court erred in holding, inferentially, that appellants had the burden of presenting such evidence in the circumstances presented.

(4) The District Court erred generally in holding that “petitioner has presented a prima facie case of relevancy and legitimacy of purpose, pursuant to the mandate of *United States v. Powell*, 379 U.S. 48, 85 S. Ct. 248, 255 (1964).”

(5) The District Court erred generally in holding that, in light of the foregoing and on the basis of the record presented, the summons issued by Brewer was authorized by Section 7602 of the Internal Revenue Code.

(6) The District Court erred in failing to dismiss the “petition” below as improper under the Federal Rules of Civil Procedure or in failing otherwise to accord appellants the benefit of the Federal Rules in treating appellees’ “petition” as a “complaint”.

SUMMARY OF ARGUMENT

Section 7602 of the Internal Revenue Code authorizes the Secretary of the Treasury or his delegate to issue a summons "[f]or the purpose of ascertaining the correctness of any return" and for certain other purposes (not here in issue under the pleadings) but *not* for any purpose at large and specifically not for criminal investigation, *i.e.*, ascertaining whether or not a crime has been committed. Section 7604 of the Code authorizes the enforcement of a summons properly issued only upon a showing that the purpose of the investigation is authorized and that compulsory production is otherwise appropriate—*i.e.*, that the material sought is relevant to a permissible investigation and is practically required (*i.e.*, that the information sought is not already available).

The showing made by appellees in this case was deficient by any meaningful standard, in effect requesting the judiciary to act as a rubber stamp enforcing the will of the person issuing the summons merely upon his assertion, without more, of the matters referred to. Indeed, the published regulation of the Internal Revenue Service describing the extent and limits of the duties of the Intelligence Division by which Special Agent Brewer is employed makes it clear that his function is solely to

"enforce the criminal statutes applicable to income . . . tax laws . . . by developing information concerning alleged criminal violations thereof, evaluating allegations and indications of such violations to determine investigations to be undertaken, investigating suspected criminal violations of such law, [and] recommending prosecution when warranted,"

and the carefully guarded evidence only confirms his concern solely with enforcement of criminal statutes. Similarly,

appellees' description of the reason why the summoned records were sought reveals on its face a lack of relevancy to the correctness of appellants' returns, loans by the Bank to appellants having no relationship to appellants' income. Moreover, the testimony offered by appellees reveals on its face that the information sought has already been ascertained by Special Agent Brewer from other records of the Bank.

If Sections 7602 and 7604 of the Code are read so as to permit enforcement of the summons upon the record in this case, a serious Constitutional issue would be raised in view of "the primary and nearly exclusive role of the Grand Jury as the agency of compulsory disclosure" required by the Fifth Amendment and the related policy of the Fourth Amendment as to the requirements pertaining to search warrants.

In any event, the procedure followed by the government in this case, directly contrary to and consciously violative of the direction of the Supreme Court in the recent case of *United States v. Powell*, 379 U.S. 48, 85 S. Ct. 248, 255, n. 8 (1964), was so deficient in depriving appellants of the benefit of the Federal Rules and depriving the court of the benefits of a full hearing following compliance with the Federal Rules that the petition should have been dismissed for such procedural defect.

ARGUMENT

I. Enforcement of the Summons Was Not, Upon the Record in This Case, Authorized by the Statute or Judicially Warranted.

Section 7602 of the Internal Revenue Code, 26 U.S.C., § 7602, provides as follows:

"For the purpose of ascertaining the correctness of any return, making a return where none has been made, determining the liability of any person for any

internal revenue tax or the liability at law or in equity of any transferee or fiduciary of any person in respect of any internal revenue tax, or collecting any such liability, the Secretary or his delegate is authorized

(1) to examine any books, papers, records, or other data *which may be relevant or material to such inquiry*;

(2) To summon the person liable for tax or required to perform the act, or any officer or employee of such person, or any person having possession, custody, or care of books of account containing entries relating to the business of the person liable for tax or required to perform the act, or any other person the Secretary or his delegate may deem proper, to appear before the Secretary or his delegate at a time and place named in the summons and to produce such books, papers, records, or other data, and to give such testimony, under oath, *as may be relevant or material to such inquiry*; and"

"(3) To take such testimony of the person concerned, under oath, *as may be relevant or material to such inquiry*." [Emphasis supplied.]

The bare minimum of proof that a delegate of the Secretary is required to produce to qualify for enforcement of a purported Section 7602 summons under Section 7604 has only recently been stated in the opinion of the Supreme Court in *United States v. Powell*, 379 U.S. 48, 85 S. Ct. 248, 255, (1964) as follows:

"He [the Commissioner] must show that the investigation will be conducted pursuant to a legitimate purpose, that the inquiry may be relevant to the purpose, that the information sought is not already within the Commissioner's possession, and that the administrative steps required by the Code have been followed—in particular, that the 'Secretary or his delegate' after investigation, has determined the further examination to be

necessary and has notified the taxpayer in writing to that effect.”*

More than that, the Court was quick to emphasize that its recitation of the bare minimum of what the government was required to show could not be read as a license to conduct a “pro forma” hearing or to use the District Courts as rubber stamps. Immediately following the portion of the opinion above quoted, the Court pointed out that:

“This does not make meaningless the adversary hearing to which the taxpayer is entitled before enforcement is ordered. At the hearing he ‘may challenge the summons on any appropriate ground,’ *Reisman v. Caplin*, 375 U.S. 440, at 449, 84 S. Ct. at 513. Nor does our

*The decision was required to settle the conflict which had developed among the circuit courts as to whether or not the government was required to show not only relevancy and materiality of its investigatory object but, more than that, “probable cause” where the taxpayer invoked the protection of Section 7605(b) of the Code prohibiting “unnecessary examination of investigations” [see and compare the circuit court decisions cited in n. 8 of the Court’s opinion] and held that, in light of the legislative history of Section 7605(b), it was not necessary for the Commissioner to meet the standard of probable cause where, to assess liability, he required information not already in his possession. Whether the Court would rule similarly where the summons, although nominally an administrative summons, was for the purpose of aiding in preparation for a criminal proceeding, however, is still subject to doubt in view of the requirements of the Fourth Amendment. *Cf. Boyd v. United States*, 116 U.S. 616 (1886) (holding the Fourth Amendment to preclude civil forfeiture proceedings based on acts of fraud against the Revenue since the proceeding “though technically of a civil proceeding, is in substance and effect a criminal one”); *In re Magnus, Mabee & Raynard, Inc.*, 311 F.2d 12, 16 (2nd Cir. 1962); *United States v. Lipshitz*, 132 F. Supp. 519 (E.D.N.Y. 1955); *Application of Myers*, 202 F. Supp. 12 (E.D. Pa. 1962); *United States v. O’Connor*, 118 F. Supp. 48 (D. Mass. 1953). For that reason, the answer of appellants to appellees’ petition sets forth as a separate defense not only that the documents sought were not relevant or material to any authorized investigation but also that there was no probable cause for issuance or enforcement of the summons, preserving the Constitutional issue in the criminal case setting here presented.

reading of the statutes mean that under no circumstances may the court inquire into the underlying reasons for the examination. It is the court's process which is invoked to enforce the administrative summons and a court may not permit its process to be abused. Such an abuse would take place if the summons had been issued for an improper purpose, such as to harass the taxpayer or to put pressure on him to settle a collateral dispute, or for any other purpose reflecting on the good faith of the particular investigation. The burden of showing an abuse of the court's process is on the taxpayer, and it is not met by a mere showing, as was made in this case, that the statute of limitations for ordinary deficiencies has run or that the records in question have already been once examined."

See also *Local 174 Etc. v. United States*, 240 F. 2d 387 (9th Cir. 1956); *Martin v. Chandis Securities Co.*, 128 F. 2d 731 (9th Cir. 1942), affirming 33 F. Supp. 478 (S.D. Cal. 1940); *United States v. Carey*, 218 F. Supp. 298, 299, n. 5 (D. Del. 1963).

The particular point that use of a summons in aid of criminal proceedings is not a permissible use under the statute is emphasized in *Reisman v. Caplin*, 375 U.S. 440, 449 (1964), where the Court said:

"Furthermore, we hold that in any of these procedures before either the district judge or United States Commissioner, *the witness may challenge the summons on any appropriate ground. This would include, as the circuits have held, the defenses that the material is sought for the improper purpose of obtaining evidence for use in a criminal prosecution.* Boren v. Tucker, 9 Cir., 239 F.2d 767, 772-773. . . ." (Emphasis supplied.)

The legislative history of Section 7602 lends further support to that strict interpretation, indicating that Section 7602 was enacted to put Internal Revenue Agents "on the

same footing as collectors with respect to the right to issue a summons to determine their primary function, i.e., the correctness of a return or the amount of the tax paid," without in any way providing any right "in Special Agents to use the summons power to seek out evidence of criminal prosecution." See Bender, *The Implications of Reisman v. Caplin in Fraud Cases*, 23rd N.Y.U. Institute on Federal Taxation, 1293, 1295-1296 (1965.)

The showing made by appellees to obtain enforcement of the summons issued by Special Agent Brewer was fatally deficient under the statute and the cases cited, however interpreted, in at least three respects.

A. APPELLEES FAILED TO PROVE THE ALLEGATION OF THE PETITION THAT BREWER'S INVESTIGATION WAS "FOR THE PURPOSE OF ASCERTAINING THE CORRECTNESS" OF APPELLANTS' INCOME TAX RETURNS.

First, there was a total lack of proof—certainly of persuasive proof—that, in the words of the Supreme Court in the *Powell* case, "the investigation [was for] a legitimate purpose." Instead, the testimony of Special Agent Brewer that his duties were "[t]o investigate alleged frauds against the Revenue" tended to confirm that the summons was to serve the illegitimate purpose (i.e., illegitimate in the sense of being unauthorized by the statute) of aiding in the enforcement of criminal statutes.

The truth of the matter—at least *prima facie* in light of the paucity of appellees' case—is best revealed by examination of the appropriate regulation of the Internal Revenue Service describing the duties and limited functions of the Intelligence Division of which Special Agent Brewer is a part, 30 Fed. Reg. 9368 (July 28, 1965), 1966 CCH Stand. Fed Tax Rep. ¶ 5988, which provides as follows:

"1118.6 Intelligence Division. The Intelligence Division enforces the criminal statutes applicable to income,

estate, gift, employment, and excise tax laws (except those relating to alcohol, tobacco, narcotics, and certain firearms), by developing information concerning alleged criminal violations thereof, evaluating allegations and indications of such violations to determine investigations to be undertaken, investigating suspected criminal violations of such laws, recommending prosecution when warranted, and measuring effectiveness of the investigation and prosecution processes. The Division assists other Intelligence offices in special inquiries, drives, and compliance programs and in the normal enforcement programs, including those combating organized wagering, racketeering, and other illegal activity, by providing investigative resources upon regional or National Office request. It also assists U.S. Attorneys and Regional Counsel in the processing of Intelligence cases, including the preparation for and trial of cases." 1966 CCH Stand. Fed. Tax Rep. ¶ 5988.

It is especially instructive to compare the function of the Intelligence Division as above described with that of the Field Audit Branch of the Audit Division, described as follows:

"1118.44 Field Audit Branch. Conducts field examinations relative to all types of taxes (except alcohol, tobacco, and firearms) to determine correct liabilities of taxpayers for tax and penalties, including the examination of claims for refund, credit or abatement, or for redemption of stamps. Also conducts field examinations of offers in compromise based on either doubt as to liability or inability to pay, and special field examinations, as requested, including joint examinations with special agents of the Intelligence Division where tax evasion may exist." 1966 CCH Stand. Fed. Tax Rep. ¶ 5988.

It is thus with both legally technical and experiential accuracy that a former Department of Justice official has

emphasized "the great distinction between the Function of an Internal Revenue Agent and a Special Agent"

"The sole function of a Special Agent in the Intelligence Division of the Internal Revenue Service is to seek evidence of crimes. He has no concern whatsoever with the amount or collection of any additional tax, these being strictly the concern of the revenue agent. He is exactly the same as any other Treasury Agent who may seek evidence of narcotics, counterfeiting, alcohol tax, customs violations, etc. A special agent is a criminal law enforcement officer, just like any state or municipal detective or policeman. He, like any other government agent who enforces the criminal law must obtain a valid search warrant."

Burns, *Searches and Seizures: The Suppression of Evidence*, N.Y.U. 20th Inst. on Fed. Tax 1081, 1087 (1962). But see the ruling on the peculiar facts presented in *Tillettson v. Boughner*, 333 F.2d 515 (7th Cir. 1964) (where the Internal Revenue Service sought merely to find out the name of the taxpayer involved and the Regulation describing the function of the Agent involved referred specifically to "the assertion of civil penalties").

In the face of such reality and upon the record presented, then, it misses the point to hold, as the District Court did, that the foregoing may be ignored because a criminal prosecution still may not result from the Special Agent's efforts. That is true, after all, with respect to any investigation made by a Treasury Agent investigating narcotics, counterfeiting or the like or any policeman investigating the occurrence of any crime. Furthermore, a criminal investigation may, and perhaps frequently does, turn up a case of civil liability (*e.g.*, an investigation of illegal sale of alcohol may reveal alcohol tax liability), but that does not make such an investigation any the less one with respect to

criminality for which administrative summonses are not permitted. Where, as here, it appears that the sole function of the person issuing the summons is to determine whether a crime has been committed, with no responsibility or function whatever as to the amount of tax payable by the person under investigation (the ascertainment of some deficiency as a requirement of criminality being his entire concern in that regard*), it cannot justify the summons under the statute that the person under investigation is in fact innocent of that, by inference, civil liability also may be of incidental interest to the investigator. Cf. *United States v. O'Connor*, 118 F.Supp. 248 (D. Mass. 1953), particularly as explained in *Boren v. Tucker*, 239 F.2d 767, 773 (9th Cir. 1956):

"The Government argued in the O'Connor case that the facts before the court showed that while 'at least one' of the purposes of the Special Agent was to aid the criminal prosecution of the taxpayer, this statement raised the *inference* that there existed other purposes, and that these other purposes might possibly be of direct interest to the Treasury and its Special Agent. The court (and we think properly so in view of the factual situation there existing) refused to consider any undisclosed purposes arising from inference, and held it to be against policy for the Judicial branch of the Government to lend its support to the use of an *unrestricted* administrative subpoena power."

Indeed, the logic and underlying reasoning supporting the foregoing view of the matter would seem irresistibly compelling were it not for the contrary argument which appellees have constructed, and which the court below apparently found persuasive, to substitute for evidence in this case the holdings on the facts presented in some other

**Herzog v. United States*, 226 F.2d 561 (9th Cir. 1955); *United States v. Schenck*, 126 F.2d 702 (2d Cir. 1942).

cases—in particular, the case of *Boren v. Tucker, supra*. Accordingly, it may be well to consider the significance of the *Boren* decision in the setting of this case.

First, it is not a holding that any investigation by any Internal Revenue Service employee or any Special Agent is to be validated by district courts merely upon request. As this Court noted in its opinion, the trial court “carefully went into the unusual factual situation”—and apparently there was relevant evidence there to consider, not a scanty record bolstered by suggested “inferences”. Thus, the instruction of that case, as much as in all the other cases which might be cited dealing with Section 7602 summons, is that, as one court explained, the “one principle in common [to] the divergent authorities” is that “the question of whether an investigation is unnecessary [or, as is challenged in this case, for a legitimate purpose] is one of fact”. [*United States v. Carey, supra*, 218 F. Supp. at 301]. If it were otherwise, the decision would have to be read as conflicting with the later decisions of the Supreme Court in the *Powell* and *Reisman v. Caplin* cases—which it is not, having indeed been cited by the Supreme Court (in *Reisman v. Caplin, supra* at 449) for the proposition that it is a sound defense to an enforcement proceeding that “the material is sought for the improper purpose of obtaining evidence for us in a criminal prosecution.”

Second, to the extent that the opinion holds to the view expressed by the court below that the possibility that a criminal prosecution may not ensue is sufficient to legitimize a Special Agent’s summons, such may be explained by the failure of the parties to fully explain to the Court in that case the sharp distinction in function between a revenue agent and a Special Agent of the Intelligence Division, revealed in this case by the published Regulations.

Third, even if the factual circumstances of the cases were the same, there has in the last ten years been a steady liberalization of the Constitutional protection afforded to those under investigation for the commission of crimes as well as those formally accused. See *Escobedo v. Illinois*, 378 U.S. 478 (1964). Here, as much or more than in the *Escobedo* case, the investigation has focused on appellants and—most clearly—there can not be any reasonable doubt that the sole function, the sole direction, the sole interest and dedication of Special Agent Brewer is to determine whether a crime has been committed and if at all possible to find that it has and to produce and put together the facts to aid in prosecution. That, under a modern view of what is permissible, should not be written off as merely harmless or possibly harmless, preliminary investigatory activity.

B. APPELLEES FAILED TO PROVE THE ALLEGATION OF THE PETITION THAT THE RECORDS SOUGHT "WOULD HAVE A DIRECT RELATION TO THE CORRECTNESS" OF APPELLANTS' RETURNS.

The only evidence offered by appellees as to the allegation of the petition that the records sought "would have a direct relation to the correctness" of appellants' returns was the testimony of Special Agent Brewer that his purpose in examining the records sought was so that he "could reconcile the difference between the loans shown by the bank as having been made to Air Conditioning Supply, and loans as shown on the books of Air Conditioning Supply as having been received from the bank." (R. 11-50.)

Allowing even every inference favorable to appellees with respect to the matter, it seems apparent as a fundamental of income tax law that the purpose and subject matter of the inquiry stated is irrelevant and immaterial to the correctness of appellants' returns: If in fact appellants borrowed more from the Bank than what their own records

show, that circumstance would not add or detract one cent from appellants' income.*

Disallowing any presumption or inference favorable to appellees from the mere fact that Special Agent Brewer asserted relevance in a general conclusionary statement in the petition (which, it may be noted, seemed to be cast in form book language), it is clear that appellees' proof is woefully deficient: Indeed, it seems a more reasonable assumption from the testimony that Special Agent Brewer desired the records referred to not to ascertain the correctness of appellants' returns but instead to ascertain the existence of one possible defense to a charge of criminal evasion.

Thus, here as much as in *Local 174, Etc. v. United States*, 240 F.2d 387, 391 (9th Cir. 1956), it would seem that:

"The tax officials assumed that all that was required upon their part was to show that they did not have sufficient data to satisfy them of the correctness of the tax returns of the Brewsters . . . and to show that possession of all of the books and documents assumed to be under control of the Local was denied them. This demand was simply that a court place the imprimatur of approval as a rubber stamp upon the administrative subpoena without further investigation. This approval would constitute the administrative enforcement officials the judges of relevance . . ."

Accordingly, it is as meet to declare again and to hold in this case that:

"The burden is upon the revenue agents in the first instance at such a judicial hearing to show that

*Conceivably the government might be legitimately interested in the amount of interest paid by appellants to the Bank if interest was taken as a deduction in an excessive amount. But it seems evident that the government does not have any interest in that subject and, indeed, it did not bother to prove even that appellants had taken any deduction for any interest payment.

the demand is reasonable under all the circumstances and to prove that the books and records which they demand are relevant or material to the tax liability of the person liable therefor . . ."

"Neither the revenue agent nor the Court has authority under the statute to require the production of memoranda, books, etc., of third parties unless they have a bearing upon the return or returns under investigation.

"In *Martin, Internal Revenue Agent v. Chandis Securities Co.*, D.C. 33 F.Supp. 478, 480, the Court, in discussing § 3614, I.R.C., said:

"The agents are not the sole judges as to the scope of the examination.

"They must satisfy the Court that what they seek may be actually needed. Otherwise, they would be assuming inquisitorial powers beyond the scope of the statute."

" . . .

"The affidavits submitted were inadequate to support propositions which the agency was required to prove, such as the materiality and relevancy of any document or item specifically described to the tax liability of either of the [taxpayers]." [240 F.2d at 390, 391.]

C. APPELLEES FAILED TO PROVE THE INFERENTIAL ALLEGATION IN SPECIAL AGENT BREWER'S AFFIDAVIT THAT THE RECORDS SOUGHT WERE REQUIRED BY HIM "IN ORDER TO ASCERTAIN THE CORRECTNESS" OF APPELLANTS' RETURNS.

As noted briefly above, Brewer's testimony in support of the petition indicated that he had somehow obtained a copy of "the bank's central liability control" with respect to loans to appellants in the years in question and that the record obtained indicated the loans made to Air Conditioning Supply Co. Thus, on the face of the record, it would appear that Special Agent Brewer already had in his possession the

basic information he said he desired to obtain; no reason was given or suggested as to why he needed or desired additional confirmation of the records he previously obtained. Accordingly, appellees failed to prove "that the information sought is not already within the Commissioner's possession" as required by *United States v. Powell*, 379 U.S. 48, 57-58 (1964). Indeed, the record, the substance of which is recited above, does not warrant the conclusion of the trial court that "there has been no evidence presented indicating that all the records and information sought belonging to the bank are 'already within the Commissioners' possession'"; to the contrary, appellees' own evidence indicated that the information sought had already been obtained.

Moreover, there does not appear to be any warrant for the inferential holding of the court below that the burden of presenting evidence with respect to what was already in Special Agent Brewer's possession was the burden of appellants. The language of the Supreme Court in the *Powell* case indicating what the Commissioner "must show" would seem to indicate that the court below was wrong as a matter of law in that regard. Cf. *Martin v. Chandis Securities Co.*, 128 F.2d 731, 735 (9th Cir. 1942), emphasizing that "[The Commissioner's] rights, if any, are statutory, and to obtain the relief granted by the statute he must bring himself within the terms thereof."

II. Enforcement of the Summons Issued Upon the Record in This Case Would Pose a Serious Constitutional Issue Under the Fourth and Fifth Amendments.

It deserves separate mention in connection with this appeal that the need to avoid impinging on delicate Constitutional rights provides added reason in this case for refusing to make any special allowance to appellees as

to the proof required to warrant enforcement of the summons. See *Application of Myers*, 202 F.Supp. 212, 213 (E.D. Pa. 1962), where the court (enjoining preliminarily the enforcement of a Section 7602 summons issued by a special agent where an indictment already had been obtained) stated that:

"We believe that Government's purpose . . . is contrary to our fundamental and deep-seated conceptions of fair play. See *United States v. O'Connor*, 118 F.Supp. 248 (D.C.Mass. 1953) . . . It should not oppress a defendant who stands accused of a crime and whose liberty is at stake . . . by invoking in aid of a criminal charge the processes which Congress has authorized for the administration of the revenue laws. The court will not permit evasion of the traditional procedure in criminal trials embodied in the Federal Rules of Criminal Procedure by resort to the great administrative powers in aid of the revenue laws which are granted by Section 7602 of the Internal Revenue Code of 1954 (26 U.S.C.A. § 7602)."

and *United States v. O'Connor*, 118 F.Supp. 248, 250-251, where Judge Wyzanski explained that:

"The Constitution of the United States, the statutes, the traditions of our law, the deep-rooted preferences of our people speak clearly. They recognize the primary and nearly exclusive role of the Grand Jury as the agency of compulsory disclosure.

"* * *

"To encourage the use of administrative subpoenas as a device for compulsory disclosure of testimony to be used in presentments of criminal cases would diminish one of the fundamental guarantees of liberty. Moreover, it would sanction perversion of a statutory power. The power under § 3614 was granted for one purpose, and is now sought to be used in a direction

entirely un contemplated by the lawgivers. The limitations implicit in every grant of power are that it will be used not colorably, but conscientiously for the realization of those specific ends contemplated by the donors of the power."

See also the searching opinion of Judge Rayfiel in *United States v. Lipshitz*, 132 F.Supp. 519 (E.D.N.Y. 1955) (suppressing use of evidence obtained by a Revenue Agent at the instance and request and for the use of a special agent in a criminal investigation).

The approval of the result in the *O'Connor* case by this Court in *Boren v. Tucker*, *supra*, would indicate, in light of the Constitutional rights referred to, the appropriateness of a similar result here.* For, in this case, just as in the *O'Connor* case unlike the situation in *Boren v. Tucker*, the government has elected (insofar as the proof is concerned) in effect to rely on merely an "inference" that Special Agent Brewer was performing some function other than the ordinary function of a policeman (to determine whether or not a crime was committed and to gather evidence for use in criminal prosecution). Indeed, as has been noted above, in view of the Treasury regulation governing Brewer's job function, if any "inference" is appropriate, it is that, just as in the *O'Connor* case and unlike the situation pre-

*The opinion of the Court in the *Boren v. Tucker* case, of course, distinguished the *O'Connor* case as factually inapplicable and, moreover, in support of the holding in favor of the enforcement of the summons there issued, the opinion indicated that the mere possibility of criminal prosecution in the future should not be a bar to investigation utilizing Section 7602. To the extent that the opinion is read to extend beyond the facts of the case, it may be in conflict, then, with the position of appellants stated in Point 1A of the Argument herein. Even if the opinion is so read, however, a different result still seems warranted here in view of the facts of the case, which, as noted in the text, *infra*, appears in context closer to the facts presented in the approved *O'Connor* case.

sented in *Boren v. Tucker*, Special Agent Brewer issued the summons solely in aid of a proposed criminal prosecution so that the District Court below (and this Court as well) has been asked in effect "to lend its support to the use of an *unrestricted* administrative subpoena power" (*Boren v. Tucker*, 239 F.2d at 773).

III. The "Petition" Should Have Been Dismissed as Improper Under the Federal Rules.

The recent decision of the Supreme Court of the United States in *United States v. Powell*, *supra*, specifically considered the manner in which enforcement of Section 7602 summons should be instituted and the governing procedure, stating as follows (n. 18):

"Because § 7604(a) contains no provisions specifying the procedure to be followed in invoking the court's jurisdiction, the Federal Rules of Civil Procedure apply, *Martin v. Chandis Securities Co.*, 9 cir., 128 F.2d 731. The proceedings are instituted by filing a complaint followed by answer and hearing. If the taxpayer has contumaciously refused to comply with the administrative summons and the Service fears he may flee the jurisdiction, application for the sanctions available under § 7604(b) might be made simultaneously with the filing of the complaint."

In proceeding by a "petition" and order to show cause obtained *ex parte*, appellees evidently chose deliberately to flout the quoted pronouncement of the Supreme Court with respect to the matter. That should have been enough in the circumstances presented to call for dismissal of the "petition", requiring appellees to commence the proceedings properly.

Nor should the District Court have deemed it an entirely satisfactory remedy merely to deem the "petition" a com-

plaint. By the ex parte order obtained, appellees, in effect, without a judicial determination focussing on the point, accomplished a suspension of the Federal Rules.* The prejudice to a respondent's trial position in such a setting is fairly obvious. What is of course more important, the impairment effected by such procedure to the administration of justice, in questing for the truth as to the matters in issue, may in circumstances be not inconsiderable.

CONCLUSION

For the foregoing reasons, the decisions below should be reversed and the District Court's order should be vacated.

February 11, 1966.

Respectfully submitted,

W. LEE McLANE

and

BROWN, VLASSIS & BAIN

By JACK E. BROWN

222 North Central Ave.

Phoenix, Arizona

Attorneys for Appellants

JACK E. BROWN

W. LEE McLANE

ARTHUR P. ALLSWORTH

Of Counsel

*It is of interest to note in that regard that, in a related enforcement proceeding brought shortly after the case here presented in which petitioners proceeded just as they did here, appellees indeed relied on an implicit suspension of the Federal Rules to argue against allowing appellants to take any depositions or the production of any documents in appellees' possession concerning Special Agent Brewer's job function, insisting that the proceeding be entirely summary in nature.

CERTIFICATE

I certify, that, in connection with the preparation of this brief, I have examined Rules 18 and 19, of the United States Court of Appeals for the Ninth Circuit, and that in my opinion, the foregoing brief is a full compliance with its rule.

JACK E. BROWN



FEB 14 1967

No. 20537

In the United States Court of Appeals
for the Ninth Circuit

ALBERT J. WILD

and

AIR CONDITIONING SUPPLY CO., INC., APPELLANTS

v.

UNITED STATES OF AMERICA, BENNETT Y. BREWER,
Special Agent

and

VALLEY NATIONAL BANK, APPELLEES

On Appeal from the Order of the United States District
Court for the District of Arizona

BRIEF FOR THE UNITED STATES AND
BENNETT Y. BREWER, SPECIAL AGENT

RICHARD M. ROBERTS,
Acting Assistant Attorney General.

LEE A. JACKSON,
JOSEPH M. HOWARD,
~~HURTON BERKLEY,~~
*Attorneys,
Department of Justice,
Washington, D. C. 20530.*

Of Counsel:

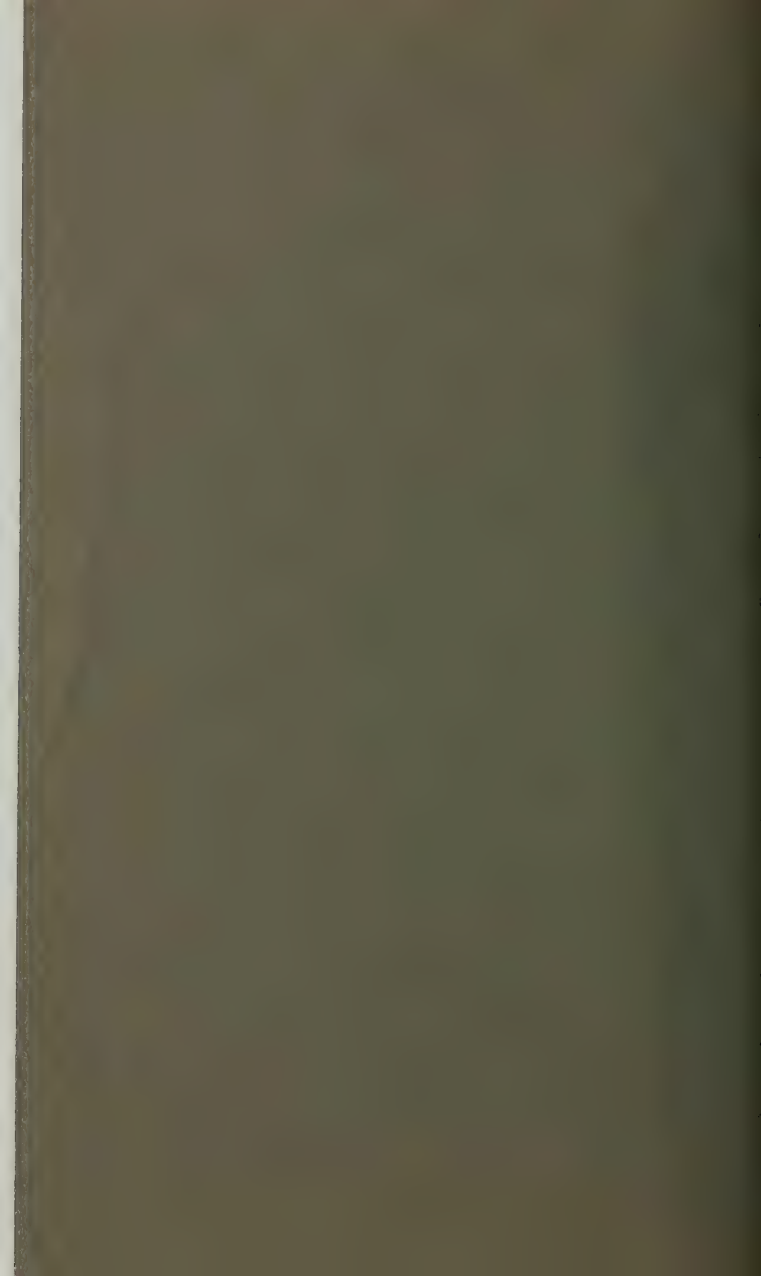
WILLIAM P. COPPLE,
United States Attorney.

RICHARD C. GORMLEY,
Assistant United States Attorney.

FILED

MAR 11 1966

WM. B. LUCK, CLERK



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**In the United States Court of Appeals
for the Ninth Circuit**

No. 20,537

ALBERT J. WILD

and

AIR CONDITIONING SUPPLY CO., INC., APPELLANTS

v.

**UNITED STATES OF AMERICA, BENNETT Y. BREWER,
Special Agent**

and

VALLEY NATIONAL BANK, APPELLEES

**On Appeal from the Order of the United States District
Court for the District of Arizona**

**BRIEF FOR THE UNITED STATES AND
BENNETT Y. BREWER, SPECIAL AGENT**

OPINION BELOW

The decision of the District Court (I R. 88-90)¹ has not been officially reported.

¹ "I R." references are to Volume I of the record on appeal, which is the court file.

JURISDICTION

This appeal involves the enforcement of an Internal Revenue summons. The Government commenced the instant action to enforce the summons pursuant to Section 7604(a) of the Internal Revenue Code of 1954. (I R. 1-3.) On July 12, 1965, the District Court entered an order to show cause why the summons should not be enforced. (I R. 8.) On July 23, 1965, the appellants moved to intervene in the action (I R. 18-19), and on July 28, 1965, they were granted leave to intervene (I R. 36). A hearing was held on July 28, 1965. (II R. 1-69.²) The court ordered enforcement on September 23, 1965 (I R. 88), and the intervenors filed their notice of appeal on October 7, 1965 (I R. 99). The respondent to the summons filed no notice of appeal. This Court's jurisdiction is invoked under 28 U.S.C., Section 1291.

QUESTIONS PRESENTED

1. Whether a special agent may issue an Internal Revenue summons in support of an investigation to ascertain the correctness of tax returns which could lead to a criminal prosecution.

2. Whether the Government's showing of materiality and relevancy was sufficient to support the court's determination that the summons should be enforced.

3. Whether the action was properly commenced procedurally.

² "II R." references are to Volume II of the record on appeal, which is the transcript of the hearing of July 28, 1965.

STATUTE, RULES, AND REGULATION INVOLVED

Section 7602 of the Internal Revenue Code of 1954, Treasury Regulations on Procedure and Administration (1954 Code), § 301.7602-1(a) and (c) (4), and Rules 1, 2, 3, 8(a) and 81(a) (3) of the Federal Rule of Civil Procedure are set forth in the Appendix, *infra*.

STATEMENT

In its petition (I R. 1-3) to enforce the instant Internal Revenue summons, the Government alleged, in relevant part, that Special Agent Brewer has been conducting an investigation of the tax returns of the appellants, Albert J. Wild and Air Conditioning Supply Co. (hereinafter referred to as taxpayers), for the years 1960 through 1962, in order to determine the correctness of those returns.³ (I R. 1.) In furtherance of this investigation the instant summons (I R. 6-7) was served on the Valley National Bank (hereinafter referred to as the bank), calling for production of certain records reflecting loan and credit transactions it had with the taxpayers, which records would have a direct relation to their tax returns for the years involved. (I R. 2.) A preliminary injunction was thereafter issued prohibiting the bank from complying with the summons until such time as the District Court might order it to be enforced.

³ The investigation began in 1963, and this Court affirmed the enforcement of an earlier summons for the production of the corporate taxpayer's books and records. *Wild v. Brewer*, 329 F. 2d 924, certiorari denied, 379 U.S. 914.

Attached to this petition was the affidavit of Agent Brewer, alleging that the instant summons was issued to secure records in support of, and which were necessary to, his investigation of the correctness of taxpayers' tax returns for the years 1960 through 1962. (I R. 4.)

In their amended answer to this position (I R. 33-34), the taxpayers⁴ denied that Agent Brewer was investigating the correctness of their tax returns, and alleged that he was actually conducting an investigation for the purpose of prosecuting or preparing to prosecute a criminal case against them. They also denied that Agent Brewer was authorized to issue summonses, and that the records sought had any relevance to the correctness of their tax returns. By way of affirmative defenses the taxpayers alleged that the petition failed to state a claim, that the records were not described with sufficient certainty, that production of the records would violate the taxpayers' Fourth and Fifth Amendment privileges, that the Government has not shown probable cause why the summons was issued or should be enforced, and the records sought had no relevance to any authorized investigation.

The case was heard before the District Court on July 28, 1965. (II R. 1.) Agent Brewer testified that he had been assigned to investigate taxpayers' tax liabilities, and that he had issued the summons to the bank to obtain loan records reflecting transactions

⁴ We are not concerned with the bank's response to this petition (I R. 25-27) in this appeal, for it has not filed any notice of appeal and is just a nominal appellee in this Court.

with the taxpayers. (II R. 47, 49.) Agent Brewer testified that he had previously examined the bank's central liability control sheets, which indicated that six or seven loans, approximating \$75,000, had been made to the corporate taxpayer, whereas the corporation's books reflected only two loans in this period totalling \$6,000. (II R. 50-53.) He testified that he wanted to examine the detailed records called for in the summons in order to obtain specific facts and figures to use in attempting to reconcile this discrepancy. (II R. 50.)

The other witness called by the Government was the custodian of the bank's credit files. (II R. 55.) He produced xerox copies of the summoned records in court and testified that they were kept in the ordinary course of the bank's business. (II R. 55-56.) He further testified that all of these records, except for the financial statements of the corporate taxpayer, had been generated by the bank. (II R. 57-58.)

Neither the bank nor the taxpayers cross-examined either witness or offered any evidence. The court took the case on briefs (II R. 68), and on September 23, 1965, ordered the bank to comply with the summons. (I R. 88-90.)

SUMMARY OF ARGUMENT

It has been held in every circuit which has considered the question, including this Court, that the Internal Revenue Service is authorized to investigate to ascertain the correctness of tax returns, and to issue

summonses in support of such investigation, even though the investigation could well lead to a recommendation for criminal prosecution. Indeed, it has been so held even where taxpayers have, in fact, been indicted subsequent to the issuance of a summons but prior to the final conclusion of the litigation concerning its enforcement. Any other rule would encourage and sanction stalling tactics. No proper Constitutional question is presented in the instant case because the records sought all belong to and are in the hands of the bank, which has not appealed, and a bank's customer has not rights or privileges concerning its records.

The Government made a proper showing of the materiality and relevancy of these records, which concerned financial transactions between the taxpayers and the bank. The lower court's factual finding on this point is supported by the facts in the record and the reasonable inferences to be drawn from them, and should be affirmed.

This Court has recognized that the Federal Rules of Civil Procedure provide that the District Court may waive their application in a case of this nature, and the court below may properly be deemed to have waived them in sanctioning the fact that the instant action was begun by filing a petition. Moreover, the petition meets all of the requirements for a complaint, and the District Court correctly held that it could be treated as such.

ARGUMENT

I.

The District Court Properly Held That A Special Agent Could Issue An Internal Revenue Summons In Furtherance Of An Investigation To Ascertain the Correctness Of Tax Returns Which Could Lead To A Recommendation For Criminal Prosecution

It is well settled in this and every other circuit which has considered this question that Section 7602 of the 1954 Code, Appendix, *infra*, authorizes the Secretary or his delegate to issue an Internal Revenue summons in any investigation to ascertain the correctness of a return or to determine tax liability, even though the investigation could well conclude with a recommendation for criminal prosecution. *Boren v. Tucker*, 239 F. 2d 767, 772-773 (C.A. 9th); *In re Magnus, Mabee & Reynard, Inc.*, 311 F. 2d 12, 16 (C.A. 2d), certiorari denied, 373 U.S. 902; *Siegel v. Tyson*, 331 F. 2d 604 (C.A. 5th); *Tillotson v. Boughner*, 333 F. 2d 515, 516-517 (C.A. 7th), certiorari denied, 379 U.S. 913; *Wright v. Detwiler*, 345 F. 2d 1012 (C.A. 3d).⁵

A special agent is expressly made one of the Secretary's delegates for this purpose. Treasury Regulations on Procedure and Administration (1954 Code),

⁵ Although the *per curiam* opinions in the *Siegel* and *Wright* cases, *supra*, do not set forth their facts, each involved an attack on the validity of an Internal Revenue summons issued by a special agent based on the same contention as the instant one. Both courts found this proposition so utterly lacking in merit that they came down with extremely quick *per curiam* opinions; the *Siegel* case was actually affirmed from the bench.

Sec. 301.7602-1(c)(4), Appendix, *infra*. An investigation involving a special agent is generally a joint investigation with a revenue agent,⁶ and the presence of the special agent merely indicates that the Service suspects the existence of civil or criminal fraud. Such an investigation could end with a determination of no deficiency, or, if a deficiency were found, there could be a recommendation for the imposition of either civil or criminal fraud penalties, or both, or neither. *Boren v. Tucker, supra*.

Nor do cases dealing with summonses issued after a taxpayer has been indicted, relied upon by the instant taxpayers (Br. 21-22), support their position. The principal case in this area is *United States v. O'Connor*, 118 F. Supp. 248 (Mass.). That case was considered at length and distinguished by this Court in *Boren v. Tucker, supra*, pointing out (239 F. 2d pp. 772-773):

The facts in the O'Connor case were vastly different from those here present. To list a few:

1. The taxpayer there was under indictment.
2. The Special Agent there, who had the subpoena issued, had at that time finished his investigation, and "completed his report".
3. The Special Agent then had no matter concerning the taxpayer pending before him.
4. The Department of Justice, (not directly, but indirectly) had "suggested" that the Admin-

⁶ Cf. *Tillotson v. Boughner, supra*, where the Seventh Circuit rejected the same contention raised herein even though the investigation was being conducted *solely* by a special agent.

istrative subpoena be used by the Special Agent to aid the Government in the preparation of the pending criminal case. The Special Agent admitted that in issuing the subpoena, "*at least one of his purposes was to aid the Department of Justice in the prosecution of the criminal case*".

5. The Special Agent, in requesting the subpoena, was in no way performing *his* duties, nor following the orders of any superior in the Internal Revenue Bureau.

The absence of these same facts also serves to distinguish the case at bar from *O'Connor*. Indeed, in *In re Magnus, Mabey & Reynard, Inc., supra*, the taxpayer was actually indicted after the service of third party summonses but before compliance therewith.⁷ The Second Circuit upheld the enforcement of the summonses, expressly following this Court's reasoning in the *Boren* opinion, and limited the *O'Connor* case and *Application of Myers*, 202 F. Supp. 212 (E.D. Pa.), strictly to their facts.

Taxpayers also mistakenly attempt to rely (Br. 11, 16) upon some language used by the Supreme Court in *Reisman v. Caplin*, 375 U.S. 440, 449. We submit that the Court was not purporting to approve the use of the instant contention as a defense to an enforcement action, but was merely enumerating types of defenses which had, at one time or another, been raised in the past. That this is the proper interpretation of the cited language is evident from the fact that the Court

⁷ This was also true in *Siegel v. Tyson, supra*.

cited *Boren v. Tucker*, *supra*, for this proposition, and in that case this Court rejected the defense.⁸

Nor is there any merit to taxpayers' contention (Br. 20-23) that enforcement of this summons affects any of their constitutional rights. The instant summons was served on the bank and it sought production of the bank's records (II R. 57-58). It is well settled that a taxpayer has no rights or privileges vis-a-vis such documents. *DeMasters v. Arend*, 313 F. 2d 79, 85 (fn. 11) (C.A. 9th), petition for certiorari dismissed, 375 U.S. 936; *Application of Cole*, 342 F. 2d 5, 7-8 (C.A. 2d), certiorari denied, 381 U.S. 950; *Zimmermann v. Wilson*, 105 F. 2d 583, 586 (C.A. 3d); *Schulze v. Rayunec*, 350 F. 2d 666, 668 (C.A. 7th), certiorari denied *sub nom. Boughner v. Schulze*, 382 U.S. 919.

The essential weakness of the taxpayers' position is high-lighted in their concession (Br. 4) that "the existence of some 'tax liability' regardless of the amount, * * * [is] an element of criminal income tax liability." It follows from this that an integral part of any administrative tax investigation, including one in which civil or criminal fraud is suspected, is the ascertainment of the correctness of the tax returns involved and the determination of the taxpayer's tax liabilities, at least to the extent of determining whether some deficiency exists. The Code authorizes the

⁸ Although it is clear that the denial of certiorari does not indicate Supreme Court approval of the lower court opinion, it might be noted that the denial of certiorari in *Tillotson v. Boughner*, *supra*, was subsequent to its decision in *Reisman*.

issuance of summonses for such purposes, and this would include that involved in the instant case.

II.

The Government Made A Sufficient Showing Of Relevancy and Materiality To Support the District Court's Determination That the Summons Should Be Enforced

The court below found that the Government "has presented a prima facie case of relevancy." (I R. 89.) This finding was manifestly a proper one, for the records sought pertain to financial transactions between the taxpayers and the bank. Taxpayers argue (Br. 17-18) that since money obtained from loans is not taxable income, these loan records would be irrelevant to the correctness of their tax returns. We submit this is not so. For example, there is the question of possible improper interest deductions adverted to by the taxpayers themselves in the footnote on page 18 of this brief. Moreover, it should be borne in mind that the individual taxpayer urged in the prior case before this Court that the corporation was merely his alter ego. *Wild v. Brewer*, 329 F. 2d 924 (dissent), certiorari denied, 379 U.S. 914. Thus the possibility arises that where the corporation has borrowed \$75,000 but only shows loans of \$6,000 on its books, the other \$69,000 may have been used by the individual taxpayer for his own purposes. If this were so, and the corporation were repaying these loans, these repayments would be constructive dividends which the individual may not have reported. Furthermore, the financial statements submitted by the corporate taxpayer to the bank may well contain

information relevant to the correctness of its tax returns.

This Court has long held that the question of materiality and relevancy is strictly one of fact (*D. I. Operating Co. v. United States*, 321 F. 2d 586, 590; *Boren v. Tucker, supra*), and in the instant case the lower court considered Agent Brewer's uncontradicted affidavit (I R. 4-5) and testimony (II R. 47-53) in making its finding of materiality. We submit this finding of fact is supported by the facts in the record and the reasonable inference to be drawn therefrom, and it should be affirmed.⁹

III

There Was No Procedural Defect in the Commencement Of the Instant Action

In *United States v. Powell*, 379 U.S. 48, 58 (fn. 18), the Supreme Court said, "Because Section 7604 (a) contains no provision specifying the procedure to be followed in invoking the court's jurisdiction, the Federal Rules of Civil Procedure apply, *Martin v. Chandis Securities Co.*, 128 F. 2d 731. The proceed-

⁹ It is difficult to see how the taxpayers can seriously contend (Br. 19-20) that the Government already has the records sought. It is obvious that the bank's central liability control (II R. 51) is some sort of summary showing nothing more than the number of loans and their amount; the records described in the summons (I R. 6) are those showing the basis for the granting of the loans, those showing amounts repaid, by whom, when, etc. To hold for the taxpayers on this point would be to say that where the Government has a business' balance sheet and income statement, it would not be entitled to look at the journals and ledgers which underlie them.

ings are instituted by filing a complaint, followed by answer and hearing." This is merely a restatement of Rule 1 of the Federal Rules of Civil Procedure, Appendix, *infra*, which sets forth the scope of the Rules, and a recognition by the Court of the absence of one of the exceptional circumstances of Rule 81 (a) (3), Appendix, *infra*, which would take such a case out from the Rules' application. However, as this Court recognized in *Chapman v. Goodman*, 219 F. 2d 802, 806, that same Rule 81(a) (3) gives the District Court the right to waive the Rules in a proceeding of this nature. Indeed, it is customary for this type of proceeding to be handled in an essentially summary manner, for Governmental requests for information should be handled with reasonable dispatch. See, e.g., *Chapman v. Goodman*, *supra*; *Boren v. Tucker*, *supra*; *United States v. Ryan*, 320 F. 2d 500, 502 (C.A. 6th), affirmed, 379 U.S. 61; see also *Porter v. Mereller*, 156 F. 2d 278, 280 (fn. 6) (C.A. 3d). Thus the court below, as in the *Chapman* case, *supra*, could be said to have partially laid aside the Rules as provided by Rule 81(a) (3), and so the commencement of this action by the filing of a petition was proper.¹⁰

Moreover, the lower court properly held that the instant petition could be treated as a complaint. Rules

¹⁰ It should be noted, (1) that Rule 81(a) (3) was not called to the attention of the Supreme Court by either party in the *Powell* case, (2) the applicability of the Federal Rules was not an issue in the *Powell* case, and (3) that this Court's 1942 decision in *Martin* antedated the 1946 amendment to that rule which clarified the authority of the district court to dispense with the Rules in enforcement proceedings. See Notes of Advisory Committee to Amendments to Rules.

2 and 3 of the Civil Rules, Appendix, *infra*, provide that a "civil action" shall be the one form of action to be brought, and it shall be commenced by filing a complaint. Rule 8(a), Appendix, *infra*, specifies that any pleading setting forth a claim for relief shall contain a short and plain jurisdictional statement, a short and plain statement of the claim showing the right to relief, and a demand for the relief sought. The petition filed by the Government to commence this action (I R. 1-3) conforms to these Rules, and, however denominated, it could be and was properly treated as a complaint. *Martin v. Chandis Securities Co.*, 128 F. 2d 731, 734 (C.A. 9th).

CONCLUSION

For the reasons set forth above the order below should be affirmed.

Respectfully submitted,

RICHARD M. ROBERTS,
Acting Assistant Attorney General.

LEE A. JACKSON,
JOSEPH M. HOWARD,
BURTON BERKLEY,
*Attorneys,
Department of Justice,
Washington, D. C. 20530.*

Of Counsel:

WILLIAM P. COPPLE,
United States Attorney.

RICHARD C. GORMLEY,
Assistant United States Attorney.

MARCH, 1966.

CERTIFICATE

I certify that, in connection with the preparation of this brief, I have examined Rules 18 and 19 of the United States Court of Appeals for the Ninth Circuit, and that, in my opinion, the foregoing brief is in full compliance with those rules.

Dated: day of, 1966.

BURTON BERKLEY,
Attorney

APPENDIX

Internal Revenue Code of 1954:

SEC. 7602. EXAMINATION OF BOOKS AND WITNESSES.

For the purpose of ascertaining the correctness of any return, making a return where none has been made, determining the liability of any person for any internal revenue tax or the liability at law or in equity of any transferee or fiduciary of any person in respect of any internal revenue tax, or collecting any such liability, the Secretary or his delegate is authorized—

(1) To examine any books, papers, records, or other data which may be relevant or material to such inquiry;

(2) To summon the person liable for tax or required to perform the act, or any officer or employee of such person, or any person having possession, custody, or care of books of account containing entries relating to the business of the person liable for tax or required to perform the act, or any other person the Secretary or his delegate may deem proper, to appear before the Secretary or his delegate at a time and place named in the summons and to produce such books, papers, records, or other data, and to give such testimony, under oath, as may be relevant or material to such inquiry; and

(3) To take such testimony of the person concerned, under oath, as may be relevant or material to such inquiry.

(26 U.S.C. 1958 ed., Sec. 7602.)

Treasury Regulations on Procedure and Administration (1954):

Sec. 301.7602-1 *Examination of books and witnesses.*

(a) *In general.* For the purpose of ascertaining the correctness of any return, making a return where none has been made, determining the liability of any person for any internal revenue tax (including any interest, additional amount, addition to the tax, or civil penalty) or the liability at law or in equity of any transferee or fiduciary of any person in respect of any internal revenue tax, or collecting any such liability, any authorized officer or employee of the Internal Revenue Service may examine any books, papers, records or other data which may be relevant or material to such inquiry; and take such testimony of the person concerned, under oath, as may be relevant to such inquiry.

* * * *

(c) *Persons who may issue summons.* The following officers and employees of the Internal Revenue Service are authorized to issue a summons pursuant to sections 6420(e)(2), 6421(f)(2), and 7602—

* * * *

(4) Intelligence; Director; assistant director; assistant regional commissioners; executive assistants to assistant regional commissioner; chiefs, Review and Conference Staff; reviewer-conferrees; chiefs and assistant chiefs of divisions, branches and sections; group supervisors; and special agents of the national, regional and district offices.

* * * *

(26 C.F.R., Sec. 301.7602-1)

Federal Rules of Civil Procedure:

Rule 1. [as amended December 29, 1948] SCOPE OF RULES

These rules govern the procedure in the United States district courts in all suits of a civil nature whether cognizable as cases at law or in equity, with the exceptions stated in Rule 81. They shall be construed to secure the just, speedy, and inexpensive determination of every action.

Rule 2. ONE FORM OF ACTION

There shall be one form of action to be known as "civil action".

Rule 3. COMMENCEMENT OF ACTION

A civil action is commenced by filing a complaint with the court.

Rule 8. GENERAL RULES OF PLEADING

(a) *Claims for Relief.* A pleading which sets forth a claim for relief, whether an original claim, counterclaim, cross-claim, or third-party claim, shall contain (1) a short and plain statement of the grounds upon which the court's jurisdiction depends, unless the court already has jurisdiction and the claim needs no new grounds of jurisdiction to support it, (2) a short and plain statement of the claim showing that the pleader is entitled to relief, and (3) a demand for judgment for the relief to which he deems himself entitled. Relief in the alternative or of several different types may be demanded.

* * * *

Rule 81. APPLICABILITY IN GENERAL

(a) *To What Proceedings Applicable.*

* * * *

(3) [as amended December 29, 1948]. In proceedings under Title 9, U.S.C., relating to arbitration, or under the Act of May 20, 1926, c. 347, § 9 (44 Stat. 585), U.S.C., Title 45, § 159, relating to boards of arbitration of railway labor disputes, these rules apply to appeals, but otherwise only to the extent that matters of procedure are not provided for in those statutes. These rules apply (1) to proceedings to compel the giving of testimony or production of documents in accordance with a subpoena issued by an officer or agency of the United States under any statute of the United States except as otherwise provided by statute or by rules of the district court or by order of the court in the proceedings, and (2) to appeals in such proceedings.

* * * *

FEB 14 1967

No. 20537

In the

United States Court of Appeals

For the Ninth Circuit

ALBERT J. WILD and AIR CONDITIONING
SUPPLY Co., INC.,

Appellants,

vs.

UNITED STATES OF AMERICA, BENNETT Y.
BREWER, and VALLEY NATIONAL BANK,

Appellees.

Reply Brief of Appellants

W. LEE McLANE

and

BROWN, VLASSIS & BAIN

222 North Central Avenue

Phoenix, Arizona

Attorneys for Appellants

JACK E. BROWN

W. LEE McLANE

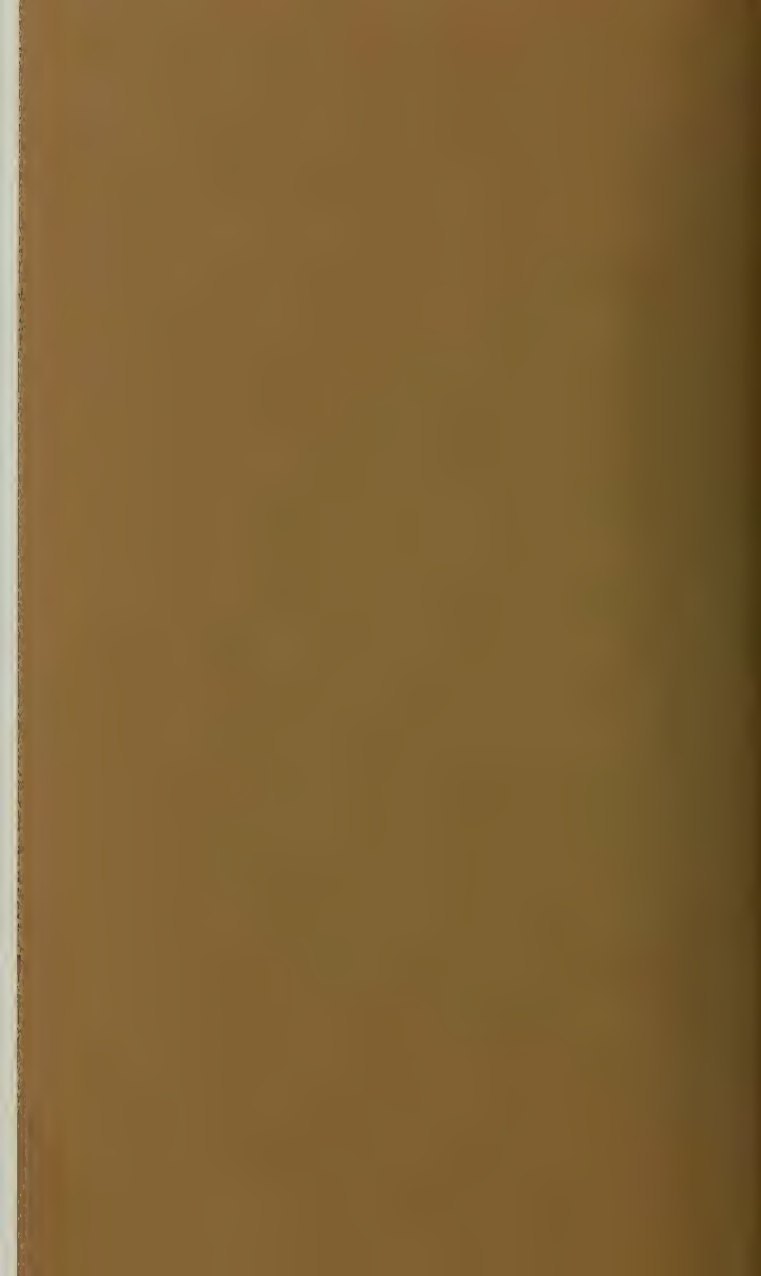
ARTHUR P. ALLSWORTH

Of Counsel

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In the
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ALBERT J. WILD and AIR CONDITIONING
SUPPLY Co., INC.,

Appellants,

vs.

UNITED STATES OF AMERICA, BENNETT Y.
BREWER, and VALLEY NATIONAL BANK,

Appellees.

Reply Brief of Appellants

I.

APPELLEES' ARGUMENT DOES NOT EXCUSE APPELLEES' FAILURE TO PROVE THAT BREWER'S INVESTIGATION WAS "FOR THE PURPOSE OF ASCERTAINING THE CORRECTNESS" OF APPELLANTS' INCOME TAX RETURNS.

The most striking, and most significant, fact concerning appellees' argument is that it fails to make any mention of the regulation of the Internal Revenue Service (published at the time Brewer's summons was issued) describing the functions of the Intelligence Division of which Special Agent Brewer is a part, 30 Fed. Reg. 9368 (July

28, 1965), cited and quoted in full in appellants' brief, pages 12-13—nor, for that matter, of Brewer's testimonial description of his job function as a criminal investigator (also quoted in appellants' brief). Appellees' argument based on victories in earlier cases involving variant facts (including a different regulation describing the function of the Intelligence Division more expansively) cannot suffice to contradict the fact in this case that Special Agent Brewer was acting here as no more and no less than a criminal investigator—like any other policeman or FBI agent; and, it is respectfully submitted, appellees' argument should not alternatively be allowed to avoid that fact. See *Local 174 Etc. v. United States*, 240 F.2d 387 (9th Cir. 1956); *Martin v. Chandis Securities Co.*, 128 F.2d 731 (9th Cir. 1942), affirming 33 F. Supp. 478 (S.D. Cal. 1940); *United States v. Carey*, 218 F. Supp. 298, 299, n. 5 (D. Del. 1963)*

Moreover, even if the case could be considered as an abstract matter without reference to the record and the illuminating regulation cited, the cases cited in appellees' brief do not necessarily support the blanket authorization the government seeks to use the administrative summons authorized by Section 7602 of the Code for any type of

*The decisions of the Supreme Court in *United States v. Powell*, 379 U.S. 48, 57-58 (1964) (quoted in appellants' brief, pages 9-11—not mentioned as to the point here involved in appellees' brief) and in *Reisman v. Caplin*, 375 U.S. 440, 449 (1964) (quoted in appellants' brief, page 11) indeed indicate that the facts here presented may not be thus ignored.

In that regard, the citation in *Reisman v. Caplin* of *Boren v. Tucker*, 239 F.2d 767, 772-773 (9th Cir. 1956), contrary to the implication drawn therefrom in appellees' brief, would seem to confirm the view expressed in *Boren v. Tucker* that it is a sound defense to an enforcement proceeding that "the material is sought for the improper purpose of obtaining evidence for use in a criminal prosecution." The Court obviously was not merely "enumerating types of defenses which . . . been raised," but types of defenses which were approved as such.

investigation, even in aid of an attempted criminal prosecution.

Apart from *Boren v. Tucker* considered in appellants' brief, pages 16-17, *Tillotson v. Boughner*, 333 F.2d 515 (7th Cir. 1964), *cert. denied*, 379 U.S. 913 (1964), involved a summons issued by a Special Agent in order to discover the name of a taxpayer on whose behalf the respondent witness had paid more than \$215,000 as a tax payment without disclosure of the name of the taxpayer or the years covered by the payment made. The use by the Special Agent of a Section 7602 summons was upheld in the peculiar circumstances presented upon the particular finding of the court that, at that time, under Section 1118.6 of the Treasury Department Statement of Organization and Functions (quoted in footnote 4 of the court's opinion, 33 F.2d at 516-517), Special Agents were authorized to investigate not only criminal matters "but also to ascertain civil penalties" [33 F.2d at 517]. Indeed, the concurring opinion of Judge Knoch specially noted that the court was proceeding on the assumptions that no criminal prosecution existed at the time the summons was issued and that Special Agents of the Intelligence Division, under the cited regulation, were authorized to ascertain civil penalties as well as investigate possible criminal violations. Thus, the *Tillotson* case points up a crucial distinction between the prior cases and this case in that the regulation governing the function of Special Agent Brewer at the time he issued the summons in this case clearly limited his function to ascertaining whether or not a violation of criminal law had occurred and to assisting in prosecutions for criminal violations.

In *Wright v. Detwiler*, 345 F.2d 1012 (3d Cir. 1965), examination of the District Court opinion which the Cir-

cuit Court affirmed *per curiam*, discloses that the court did not focus at all upon the question here involved but instead upon the right of the taxpayers in that case to resist production of the records of their family-owned corporation under the privilege of the Fifth Amendment and related rights under the Fourth Amendment. Insofar as the point here involved may have been raised, it is especially noteworthy that the evidence produced by the government at the enforcement hearing consisted of testimony by a revenue agent (rather than the Special Agent) who testified sufficiently to persuade the court that "a genuine tax liability investigation" was involved [241 F. Supp. at 755].

In *In re Magnus, Mabee & Reynard, Inc.*, 311 F.2d 12 (2d Cir. 1962), *cert. denied*, 373 U.S. 902 (1963), the court particularly noted that the summonses involved were issued at a time when a Special Agent was "just beginning his investigation of the taxpayers' returns" and at a time when no conclusion could have been made as to whether any criminal action was indicated (an indictment having apparently been obtained some ten months subsequently merely to prevent the statute of limitations against criminal prosecutions from running). Indeed, it appears that the investigation involved a taxpayer who did not file any income tax returns for a period of nine years and that

"Through the issuance of the summons, the *revenue agents* sought to obtain access to the corporation's books to ascertain what taxes, if any, should have been reported by the taxpayers for the years in question. . . ." [311 F.2d at 14, emphasis supplied.]

In short, in the cases cited by the government as well as in any other case conceivable, the "one principle in common [to] the divergent authorities" is that the question of

whether an investigation is for the purpose alleged by the government in seeking enforcement "is one of fact" [*United States v. Carey*, 218 F. Supp. 298, 301 (D. Del. 1963).]

Nor may the serious Constitutional question which the breadth of appellees' argument would raise be avoided by ignoring the question and instead arguing some other case, as appellees' brief does. The Constitutional limitations upon "the use of an *unrestricted* administrative subpoena power" [*Boren v. Tucker*, 239 F.2d at 773], regardless of the nature of the investigation as a criminal investigation, has been too well stated in *United States v. O'Connor*, 118 F.Supp. 248 (D.Mass. 1953), *Application of Myers*, 202 F.Supp. 212, 213 (E.D.Pa. 1962) and *United States v. Lipshitz*, 132 F. Supp. 519 (E.D.N.Y. 1955) to be so lightly dismissed or avoided. *Cf.* also the required according of Constitutional rights when an investigation "has begun to focus on a particular suspect" and has become in effect accusatory in nature, *Escobedo v. Illinois*, 378 U.S. 478, 490 (1964), which recently has been persuasively defined in the context of tax investigation as applicable when a Special Agent of the Intelligence Division appears on the scene, as follows:

"The next step in the fraud investigation is the appearance of the Special Agent. In its broadest interpretation the 'investigation' is not necessarily concluded by the appearance of the Special Agent on the scene. Indeed, frequently the Special Agent's task is merely to obtain evidence, oral and written, which may be used against that particular taxpayer in a criminal prosecution. The effect, then, is to shift, at a point not later than his appearance, the investigatory process to one of accusation—truly no different than the interrogation of a defendant after arrest in a non tax fraud criminal case. At this point, since there is unquestionably a criminal 'investigation' underway and henceforth since any information which is obtained from the

taxpayer will be obtained with an eye toward possible criminal sanctions, there is clearly a focusing on that particular taxpayer as the suspect and no one else. It is submitted that the right to counsel should attach no later than at the appearance of the Special Agent."

Hewitt, *Sixth Amendment Rights of the Taxpayer in a Fraud Investigation*, ABA Bulletin of the Section of Taxation 90, 121-122 (Jan. 1966). But see *Kohatsu v. United States*, 65-2 USTC ¶ 9715 (9th Cir. 1965).

Finally, what appellees have otherwise missed can hardly be supplied by attempting to build upon the explanation in appellants' brief that the existence of some "tax liability", regardless of the amount, is one premise of a criminal income tax case. As explained in appellants' brief read in context, that fact cannot convert Brewer's function from that of a criminal investigator to that of a revenue agent who may truly be engaged in ascertaining the correctness of an income tax return. It bears re-emphasis that, no matter how much appellees may ignore what the regulation makes clear as a matter of law and fact and no matter with what cleverness appellees may attempt to circumvent the fact, the fact remains that Brewer was and is engaged in nothing more and nothing less than criminal investigation unauthorized by Section 7602 of the Code (and, if not, proscribed by the Constitutional provisions pertaining to criminal investigations).

II.

APPELLEES' ARGUMENT DOES NOT EXCUSE APPELLEES' FAILURE TO PROVE THAT THE RECORDS SOUGHT "WOULD HAVE A DIRECT RELATION TO THE CORRECTNESS" OF APPELLANTS' RETURNS AND THAT THE RECORDS SOUGHT ARE REQUIRED FOR THAT PURPOSE.

Appellees' imaginative argument as to why the records sought might have some relation to the correctness of ap-

pellants' returns falls far short of the showing required by any meaningful standard. As for "possible improper interest deductions", appellees did not bother to prove even that appellants had taken any deduction for any interest payment. As for the speculation that if loans were used by the individual taxpayer and were repaid by the corporation there might be constructive dividends, first, the testimony did not advert to any such possibility, and second, the reason for that lapse may well have been that in fact Brewer already had information defeating that remote possibility. (It will be recalled that Brewer testified that he had already obtained in some way "the bank's central liability control with respect to these two borrowers" [Tr., p. 52]; so far as appears, the document thus already viewed by Brewer gave him all the information relevant to any such issue.)

Thus, in this case at least as much as in *D.I. Operating Company v. United States*, 321 F.2d 586 (9th Cir. 1963), Brewer's conclusionary affidavit, placed in issue by the pleadings, and his slight, inconclusive testimony, must be viewed as "inadequate to support the lower court's order." See also *Local 174 Etc. v. United States*, 240 F.2d 387, 390-391 (9th Cir. 1956); cf. *Martin v. Chandis Securities Co.*, 128 F.2d 731, 735 (9th Cir. 1942).

III.

APPELLEES' ARGUMENT DOES NOT EXCUSE THE DEPRIVATION OF APPELLANTS' RIGHTS UNDER THE FEDERAL RULES EFFECTED WITHOUT A JUDICIAL DETERMINATION SUSPENDING THE RULE.

Appellees' argument that their deliberate flouting of the direction of the Supreme Court in *United States v. Powell* that enforcement proceedings such as that here involved should be instituted under the Federal Rules "by filing a complaint, followed by answer and hearing" may be exe-

cuted by reference to Rule 81(a)(3) ignores the fact that at no time did appellees request the court below to order a suspension of the Federal Rules and at no time was such an order entered. Thus, there is no occasion for this Court to consider whether or not such an order would have been appropriate if it had been entered. The cases cited by appellees, all decided prior to the Supreme Court decision in the *Powell* case, can hardly be viewed as having any bearing on the proceedings here involved in the circumstances.

Nor can appellees' self-decreed suspension of the Rules be excused by the court's deeming the "petition" a complaint after the fact, *i.e.*, after a summary hearing was had and the benefits which appellants would have had from the Federal Rules if the proceedings in fact had been commenced by a complaint (particularly the benefit of pre-trial discovery, which would have enabled appellants to develop additional facts in aid of their position contradicting Brewer's conclusionary allegations) had in effect been denied to them.*

*Nor, of course, should it avail appellees to argue here, as apparently they intend to argue, that the *Powell* decision was wrong. If it was, appellees have more than the usual opportunity afforded to a litigant to have the matter reheard by the Supreme Court. Meanwhile, it seems only fitting that appellees as much as other litigants should be bound to proceed in accordance with so clear a directive so recently issued and, at least, not to circumvent it by ignoring it and then contending that a suspension of the Rules, which they failed to apply for, can be implied. *Cf.* the pungent comment of Mr. Justice Jackson that

"It is very well to say that those who deal with the Government should turn square corners. But there is no reason why the square corners should constitute a one-way street." *Rodgers v. United States*, 332 U.S. 380, 387-88 (1947) (dissenting opinion.)

CONCLUSION

For the foregoing reasons, the decision below should be reversed and the District Court's order should be vacated.

March 30, 1966.

Respectfully submitted,

W. LEE McLANE
and
BROWN, VLASSIS & BAIN

By JACK E. BROWN

222 North Central Avenue
Phoenix, Arizona

Attorneys for Appellants

JACK E. BROWN
W. LEE McLANE
ARTHUR P. ALLSWORTH

Of Counsel

CERTIFICATE

I certify, that, in connection with the preparation of this brief, I have examined Rules 18 and 19, of the United States Court of Appeals for the Ninth Circuit, and that in my opinion, the foregoing brief is a full compliance with its rule.

JACK E. BROWN

FEB 14 1967

No. 20544 ✓

In the

United States Court of Appeals

For the Ninth Circuit

STOCKTON PORT DISTRICT,

Petitioner,

vs.

FEDERAL MARITIME COMMISSION and UNITED
STATES OF AMERICA,

Respondents.

Opening Brief of Petitioner Stockton Port District

ALBERT E. CRONIN, JR.

320 Wells Fargo Bank Building
Stockton, California 95202

J. RICHARD TOWNSEND

Route 2, Box 294,
Martinez, California 94553

*Attorneys for Petitioner
Stockton Port District*

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No. 20544

In the

United States Court of Appeals

for the Ninth Circuit

STOCKTON PORT DISTRICT,

Petitioner,

vs.

FEDERAL MARITIME COMMISSION and UNITED
STATES OF AMERICA,

Respondents.

Opening Brief of Petitioner Stockton Port District

A.

The Court's Jurisdiction

This proceeding involves a petition to review and set aside, in part, a final order of the Federal Maritime Commission (hereinafter referred to as the Commission) entered under authority of the Shipping Act, 1916 (46 U.S.C. 801 et seq.). Petitioner Stockton Port District was the complainant in the proceeding before the Commission and, as is explained hereinafter, has been aggrieved by the Commission's order.

Sections 2 and 4 of the Review Act of 1950 (5 U.S.C. 1032, 1034) give the United States Court of Appeals exclusive jurisdiction to review such a final order pursuant to a petition filed by a party aggrieved by the order. Jurisdiction herein is based on such statutory provisions.

Venue herein is based on Section 3 of the Review Act of 1950 (5 U.S.C. 1033), which provides that the venue of such a proceeding shall be in the judicial circuit wherein the petitioner has its residence or principal office. Petitioner Stockton Port District is a public corporation whose principal place of business and principal office are located at Stockton, California, in the Ninth Circuit.

B.

Statement of the Case

The decision of the Commission here under review will, unless set aside by the Court, have a far-reaching disastrous effect on various ports throughout the United States. The "port equalization" device which has been approved by the Commission's decision permits steamship lines to use a port developed with Government funds for rate-making purposes and to deprive it of cargo which it would otherwise receive by diverting the cargo to another port for loading by means of a rebate to the shipper of part of his inland transportation charges.

By approving the device of "port equalization" the Commission's decision gives the Conference steamship lines, and indeed even foreign steamship lines, the power to determine which ports in the United States shall prosper and which shall be deprived of cargo that they would normally receive—in direct opposition to the expressed Congressional policy of encouraging the use by vessels of ports for cargo

which would naturally pass through them*, and in spite of the expenditure of millions of dollars of Government funds toward the development of the ports which will be adversely affected.

Petitioner Stockton Port District is a public corporation organized under the laws of the State of California and is a political subdivision. Petitioner and the City of Stockton, California, a municipal corporation, own the wharves and other facilities comprising the Port of Stockton, which are operated by petitioner. The Port of Stockton is located in the San Joaquin Valley 84 miles by water from the Golden Gate. (Rep. Tr. 8, 30, Phelps.)†

On or about December 27, 1962, petitioner filed a complaint with the Federal Maritime Commission pursuant to the Shipping Act, 1916, (46 U.S.C. 801 et seq.), in which the Pacific Westbound Conference, the Pacific Straits Conference, the Pacific/Indonesian Conference, and the individual members of such Conferences were named as respondents. Such Conferences are voluntary associations of steamship lines operating pursuant to agreements approved by the Commission or its predecessor under Section 15 of the Shipping Act, 1916 (46 U.S.C. 814). The complaint before the Commission was entitled Stockton Port District v. Pacific Westbound Conference, et al., and was assigned Docket No. 1086.

In its complaint before the Commission petitioner alleged that certain provisions of the tariffs of such Conferences and their members which permit "port equalization", and the practices of the Conferences and their members with

*See Section 8 of Merchant Marine Act, 1920, (46 U.S.C. 867).

†References to the testimony of witnesses before the Commission in the Reporter's Transcript will be cited in this manner. Such Reporter's Transcript is the first document set forth in the Court Record and the page numbers of the Reporter's Transcript are the same as the pages of the Court Record.

respect to port equalization against the Port of Stockton, are unlawful on various grounds which are discussed hereinafter.

Port equalization is a device whereby, instead of loading cargo at the port nearest the origin of the cargo, an ocean carrier diverts the cargo to a more distant port for loading by paying the shipper a rebate equal to the difference in his inland transportation charges to the respective ports. Under port equalization the shipper's inland transportation charges are, by means of such rebate by the ocean carrier, made the same to the port at which the cargo is loaded as the inland transportation charges which the shipper would have incurred if the cargo had moved over the port to which the lowest inland transportation charges apply from the point of origin of the cargo.

Under the practice of port equalization in which these Conferences and their members engage, for example, if the inland transportation charge from Fresno, California, to the Port of Stockton on certain cargo is 20 cents per 100 pounds, and the corresponding charge to San Francisco, California, is 30 cents, the ocean carrier members of these Conferences are permitted by their tariffs to load, and do load, such cargo at San Francisco and pay 10 cents per 100 pounds of the shipper's inland transportation charges to San Francisco, so that the shipper's inland transportation charges will be the same as though his cargo had been loaded at the port to which the lowest inland transportation charges apply, which is Stockton.

The effect of such port equalization is to deprive the Port of Stockton of a substantial volume of cargo which would move over that port in the absence of the port equalization. To the extent that such cargo would have moved over the Port of Stockton without the port equalization, that port

has lost revenue from terminal charges on such cargo which it would otherwise have received. (See Commission's Report, page 5, R. 1270.)* Information supplied by the Conferences shows that in 1962—the latest year available—a total of 47,529 tons of cargo was equalized against the Port of Stockton by the members of these Conferences. (Ex. 11-14.) The Commission found that "Without equalization much of the cargo would move through Stockton". (Com. Rep. 7-8, R. 1272-73.) Of the 47,529 tons equalized against the Port of Stockton in 1962, 1,400 tons moved over the Ports of Los Angeles and Long Beach, and the balance of 46,129 tons moved over San Francisco Bay ports, nearly all over San Francisco. (Ex. 11-14.) Of the total of 47,529 tons equalized against Stockton, 44,136 tons moved via members of the Pacific Westbound Conference and 3,393 tons via members of the Pacific Straits and Pacific/Indonesian Conferences. (Ex. 11-14.)

The port equalization rules of the Conferences here involved are set forth as Appendix A hereof in the same form in which they were set forth as Appendix A of the Commission's Report, with the portions relating particularly to the Port of Stockton being underscored as underscored by the Commission.

In and by its Report and Amended Order† in Docket No. 1086, the Commission found and concluded that the port equalization rules of these Conferences and their members, and practices in accordance therewith, are *unjustly discriminatory and unfair* to the Port of Stockton and ports

*The pages of the Commission's Report will be cited as "Com. Rep. 5" etc. References to the Transcript of the Record before the Court will be cited as "R. 1270" etc. Exhibits will be cited as "Ex.").

†The "Amended Order" will be referred to herein as "the Order". It superseded the original Order and is the same as the original Order, except that it includes a performance date which was left blank in the original order.

on San Francisco Bay, and hence in violation of Section 15 of the Shipping Act, 1916, (46 U.S.C. 814), to the extent that they provide for equalization of inland transportation against the Port of Stockton and ports on San Francisco Bay *on cargo loaded at Los Angeles and Long Beach, California.*

The majority of the Commission found and concluded, however, that the port equalization rules and practices of the Conferences involved and their members are *not unlawful* in the case of port equalization against the Port of Stockton *on cargo loaded at San Francisco or any other port located on San Francisco Bay.** This distinction between cargo loaded at Los Angeles and Long Beach and at a port located on San Francisco Bay was based on the unsupportable and completely irrelevant grounds (a) that Stockton and San Francisco are both San Francisco "bay area" ports and consequently are both in the same "geographical area", and (b) that the area which is "naturally" tributary to Stockton is also "naturally" tributary to San Francisco.

The dissenting report of Commissioner Hearn condemns the decision of the majority of the Commission because it results in "(1) frustrating the will of Congress in developing new and modern ports and (2) turning over to conference carriers, the right to determine which of our ports shall prosper and which shall suffer." (Com. Rep. 28, R.

*The Commission's Report was issued by three of the five Commissioners. It was accompanied by a dissenting opinion of Commissioner Hearn, who concurred in the conclusion that port equalization against Stockton on cargo loaded at Los Angeles and Long Beach is unlawful, but who dissented vigorously with respect to the conclusion that port equalization against Stockton on cargo loaded at a San Francisco Bay port is lawful. The Commission's Report states (page 33, R. 1299) that Commissioner Patterson "concurs in the result" and will issue a supplemental report. His supplemental report was issued after the Petition for Review herein was filed, namely on January 21, 1966.

1294.) *The dissenting report also concludes that Stockton is not a San Francisco Bay area port, that cargoes naturally tributary to Stockton are not "naturally" tributary to San Francisco, and that undue prejudice against the Port of Stockton results from the fact that most of the cargo which is equalized against Stockton and loaded at San Francisco would move via Stockton in the absence of the equalization.* (Com. Rep. 30-32, R. 1296-98.) *The dissenting report holds that "the subject equalization rules against Stockton are violative of Section 16 First of the Shipping Act, contrary to the public interest standard of Section 15, and in contravention of the principles and policies of Section 8 of the Merchant Marine Act, 1920, and Section 205 of the Merchant Marine Act, 1936."* (Com. Rep. 27A-28, R. 1293-94.)

This Petition for Review is directed toward the failure of the Commission to conclude that the port equalization here involved against the Port of Stockton on cargo loaded at San Francisco or any other port on San Francisco Bay is unlawful, and the Commission's failure to order the Conference tariff rules amended accordingly.

C.

Specification of Errors

The errors in the Commission's Report and Order which are relied upon by petitioner are as follows:

1. The Federal Maritime Commission (the Commission) erred in concluding that port equalization against the Port of Stockton as practiced by the respondents before the Commission on cargo loaded at San Francisco or any other port located on San Francisco Bay is lawful.

2. Having concluded that port equalization against the Port of Stockton on cargo loaded at Los Angeles

and Long Beach is unlawful (Com. Rep. 25-27A, R. 1290-93), the Commission erred as a matter of law in failing to conclude that port equalization against the Port of Stockton on cargo loaded at San Francisco or any other port located on San Francisco Bay is likewise unlawful.

3. The Commission's finding and conclusion that Stockton and San Francisco are both San Francisco "bay area" ports and are both in the same "geographical area" (Com. Rep. 12, R. 1277) are unsupported by substantial evidence.

4. The Commission's finding and conclusion that the territory which is "naturally" tributary to Stockton should properly be considered "naturally" tributary to San Francisco and other San Francisco Bay area ports (Com. Rep. 16, R. 1281) are unsupported by substantial evidence.

5. The Commission's conclusion that "the territory surrounding Stockton and the entire Bay area is centrally, economically and naturally served by the conference facilities at San Francisco" (Com. Rep. 16, R. 1281) is unsupported by adequate findings and unsupported by substantial evidence.

6. Even if it could be said that Stockton and San Francisco are both "bay area" ports and are both in the same geographical area, and that the area which is naturally tributary to Stockton is also naturally tributary to San Francisco, the Commission erred as a matter of law in concluding that those factors preclude unfairness, unjust discrimination and undue prejudice against Stockton and a violation of the policy of Section 8 of the Merchant Marine Act, 1920, (46 U.S.C. 867), and in failing to conclude that the legal issue involved in determining whether such violations

of law result from port equalization is whether the equalization results in the movement via San Francisco of cargo that would move via Stockton if it were not for the equalization.

7. Having found that "Without equalization much of the cargo would move through Stockton" (Com. Rep. 7-8, R. 1272-73), the Commission erred as a matter of law in failing to find and conclude that port equalization by the respondents before the Commission results in unfairness, unjust discrimination and undue prejudice against Stockton on cargo loaded at San Francisco and other ports on San Francisco Bay, in violation of Sections 15 and 16 (First) of the Shipping Act, 1916, (46 U.S.C. 814, 815), and violates the policy of Section 8 of the Merchant Marine Act, 1920, (46 U.S.C. 867), and is hence contrary to the public interest and in violation of Section 15 of the Shipping Act, 1916, (46 U.S.C. 814).

8. Having found that "if there were no equalization, many perishable commodities would still move through San Francisco rather than Stockton" (Com. Rep. 8, R. 1273) and that "not all the equalized cargo would have gone to Stockton but for equalization" (Com. Rep. 14, R. 1279), the Commission erred as a matter of law in failing to conclude that port equalization against the Port of Stockton on cargo loaded at San Francisco and other ports on San Francisco Bay results in rebates by the respondents before the Commission to shippers whose cargo would move via a San Francisco Bay port in the absence of such port equalization, in violation of Section 16 (Second) of the Shipping Act, 1916, (46 U.S.C. 815).

9. The Commission erred as a matter of law in concluding that port equalization against Stockton on

cargo loaded at a port on San Francisco Bay is not contrary to the public interest, in violation of Section 15 of the Shipping Act, 1916, (46 U.S.C. 814), because it is beneficial to shippers and the carriers which equalize against Stockton (Com. Rep. 20-22, R. 1285-87), and in failing to conclude that it is contrary to the public interest, in violation of said Section 15, because it is detrimental to the Port of Stockton and to carriers which serve or desire to serve Stockton.

10. Having found that "Although equalization is optional under the tariff, carriers find that competition compels them to equalize" (Com. Rep. 8, R. 1273), the Commission erred as a matter of law in failing to conclude that port equalization as practiced by the respondents before the Commission against the Port of Stockton on cargo loaded at a San Francisco Bay port prevents a respondent from serving the Port of Stockton as its managerial judgment dictates, in violation of Section 205 of the Merchant Marine Act, 1936, (46 U.S.C. 1115).

11. The Commission erred as a matter of law in concluding that the prior decisions support its position.

12. The Commission erred as a matter of law in concluding (Com. Rep. 23, R. 1288) and ordering (R. 1301, 1305) that the respondents before the Commission should remove the language "which would normally move" from the rule, since the Commission's interpretation of such language is unsupported by substantial evidence and since this will result in a clear rebate to shippers who would move their cargo via San Francisco without any equalization, in violation of Section 16 (Second) of the Shipping Act, 1916, (46 U.S.C. 815).

13. The Commission's conclusions with respect to the lawfulness of equalization against Stockton on

cargo loaded at San Francisco or any other port on San Francisco Bay are based on findings which are unsupported by substantial evidence, and on errors of law, and are unsupported by adequate findings.

14. The Commission's Amended Order served on September 28, 1965, (R. 1304-05), is unlawful to the extent that it fails to conclude that port equalization against the Port of Stockton on cargo loaded at San Francisco or any other port on San Francisco Bay is unlawful, in violation of Sections 15 and 16 (First) and (Second) of the Shipping Act, 1916, (46 U.S.C. 814, 815), of the policy declared in Section 8 of the Merchant Marine Act, 1920, (46 U.S.C. 867), and of Section 205 of the Merchant Marine Act, 1936, (46 U.S.C. 1115), and to the extent that it fails to order the respondents before the Commission to cease and desist from applying their equalization rules to such cargo and to modify their equalization rules to exclude their application to cargo loaded at such ports which is equalized against the Port of Stockton.

15. The Commission's Report and Amended Order are arbitrary, capricious, and an abuse of the Commission's power and discretion to the extent that they fail to conclude that port equalization against the Port of Stockton on cargo loaded at a port located on San Francisco Bay is unlawful.

16. The Amended Order served on September 28, 1965, deprives petitioner Stockton Port District of property without due process of law, in violation of the Fifth Amendment to the Constitution of the United States, in that it improperly permits the respondents before the Commission to deprive petitioner of revenue which it would receive in the absence of the port equalization.

Argument

I.

SUMMARY OF ARGUMENT

Petitioner's argument may be summarized briefly as follows:

1. *Violation of Policy of Section 8 of Merchant Marine Act, 1920.*—Section 8 of the Merchant Marine Act, 1920, (46 U.S.C. 867), expresses a Congressional policy of encouraging the use by vessels of ports for cargo which would naturally pass through them.* The Commission's decision violates this policy in two respects: First, by approving the "port equalization" against the Port of Stockton on cargo loaded at San Francisco or any other port on San Francisco Bay, the decision permits ocean carriers to divert from the Port of Stockton cargo which would naturally pass through that port except for the rebate paid to the shipper for sending his cargo to a port other than Stockton. Second, in considering the public interest, the Commission's decision (Com. Rep. 20-22, R. 1285-87) considers only the interest of shippers and of the ocean carriers which equalize against Stockton instead of sending their vessels to Stockton, and disregards completely the interest of the Port of Stockton and of ocean carriers which serve or desire to serve Stockton, and the detrimental effect on such port and carriers. The port equalization which has been approved in violation of such Congressional policy in these two respects is therefore contrary to the public interest and in violation of Section 15 of the Shipping Act, 1916, (46 U.S.C. 814).

*The provisions of all of the statutes which are relied upon by petitioner in support of its position are set forth in Appendix B of this Brief.

2. *Violation of Section 205 of Merchant Marine Act, 1936*.—Section 205 of the Merchant Marine Act, 1936, (46 U.S.C. 1115), makes it unlawful for any conference or ocean common carriers to prevent any other such carrier from serving any port of the type of the Port of Stockton. Port equalization as practiced by the Conference carriers here involved against the Port of Stockton on cargo loaded at a San Francisco Bay port prevents such carriers from serving the Port of Stockton as their managerial judgment dictates. This constitutes a violation of Section 205 by the Conferences which maintain the port equalization rules in their tariffs.

3. *Rebate in Violation of Section 16 (Second) of Shipping Act, 1916*.—Some of the equalization payments under consideration are made to shippers whose cargo would move via a San Francisco Bay port *even if there were no equalization*. Such equalization payments constitute an unlawful rebate, in violation of Section 16 (Second) of the Shipping Act, 1916, (46 U.S.C. 815).

4. *Unfairness, Unjust Discrimination and Undue Prejudice Against Port of Stockton*.—The Commission correctly concluded that when the inland transportation rate from the origin of the cargo, such as Fresno, is less to Stockton than to Los Angeles and Long Beach, port equalization by the respondent Conferences and their members against the Port of Stockton on such cargo when it is loaded at Los Angeles or Long Beach is unlawful, since it deprives Stockton of cargo which would move over that port in the absence of such equalization. Such port equalization was held to be unjustly discriminatory and unfair between ports, in violation of Section 15 of the Shipping Act, 1916, (46 U.S.C. 814). (Com. Rep. 25-27A, R. 1290-93.)

Yet when the inland transportation rate on the same cargo from the same point of origin is less to Stockton than

to San Francisco and the cargo is loaded at San Francisco, the majority of the Commission has held that port equalization against Stockton is entirely lawful, even though the cargo would have moved over the Port of Stockton in the absence of such equalization and the equalization deprives Stockton of the cargo.

What are the reasons given by the majority of the Commission for such obviously inconsistent conclusions? First, that Stockton and San Francisco are both San Francisco "bay area" ports and are hence both in the same "geographical area". (Com. Rep. 12, R. 1277.) And second, that the territory which is "naturally" tributary to Stockton should properly be considered "naturally" tributary to San Francisco and other ports on San Francisco Bay. (Com. Rep. 16, R. 1281.) Commissioner Hearn has registered a vigorous dissent to this completely unfounded distinction between cargo loaded at Los Angeles and cargo loaded at San Francisco. (Com. Rep. 27A-33, R. 1293-99.)

We shall show that this attempted distinction in port equalization against Stockton on cargo loaded at San Francisco and at Los Angeles is wholly unsupported in fact and in law. Having correctly concluded that port equalization against Stockton on cargo loaded at Los Angeles and Long Beach is unlawful, the Commission should have concluded that port equalization against Stockton on cargo loaded at San Francisco or any other port located on San Francisco Bay is likewise unlawful.

These respective grounds of unlawfulness of the port equalization against the Port of Stockton on cargo loaded at a San Francisco Bay port will be discussed in the order stated. In such discussion we shall show that the conclusions of the Commission to the contrary are based on findings and conclusions which are unsupported by substantial

evidence, and on errors of law, and are unsupported by adequate findings. We shall likewise show that the Commission's conclusion (Com. Rep. 23, R. 1288) and order (R. 1301, 1305) that the language "which would normally move" over another port be removed from the equalization rule is based on findings which are unsupported by substantial evidence and on an error of law. Finally, it will be shown that the Commission's Order deprives petitioner of property without due process of law, in violation of the Fifth Amendment to the Constitution of the United States, by improperly permitting the respondents before the Commission to deprive petitioner of revenue in the form of terminal charges which it would receive from cargo that would move over the Port of Stockton in the absence of the port equalization.

Annexed to this Brief as Appendix C is a table showing page references to the record where exhibits presented before the Commission were identified, offered and received or rejected as evidence.

II.

VIOLATION OF POLICY OF SECTION 8 OF MERCHANT MARINE ACT, 1920

The Commission's decision violates the policy expressed by Congress in Section 8 of the Merchant Marine Act, 1920, (46 U.S.C. 867), in two respects, which will be discussed separately.

a. Diversion of Cargo from Port of Stockton.

We have seen that 47,529 tons of cargo were equalized by the respondent Conference lines against the Port of Stockton in 1962, and that of this amount 46,129 tons moved over ports located on San Francisco Bay. (Ex. 11-14.) The

Commission has found that "Without equalization much of the cargo would move through Stockton". (Com. Rep. 7-8, R. 1272-73.) Moreover, the respondent Conferences' equalization rules* allow equalization only under the following circumstances:

"* * * cargo which would normally move from one California terminal port, may be shipped under equalization via another California terminal port." (See paragraph (e) of Appendix A hereof. Emphasis supplied.)

The equalization rules and practices which have been approved by the Commission, therefore, clearly decrease and discourage the use of the Port of Stockton for cargo that would otherwise normally and naturally pass through that port.

In the case of *Pacific Far East Line v. United States*, 246 F. (2d) 711 (C.A., D.C. 1957) the United States Court of Appeals upheld a decision of the Federal Maritime Board in *City of Portland v. Pacific Westbound Conference*, 4 F.M.B. 664 (1955), which held that port equalization against ports in Oregon and Washington on certain products loaded at California ports was "unjustly discriminatory and unfair as between ports within the meaning of Section 15 of the Act and detrimental to the United States *as contrary to the principles of Section 8 of the Merchant Marine Act*" (emphasis supplied), since it resulted in diversion of traffic which otherwise would naturally pass through the complaining ports. (See 246 F. (2d) 714.) In upholding the Board's decision, the Court relied on the policy of Congress expressed in Section 8 of the Merchant Marine Act, 1920. With respect to Section 8 of that Act the Court said:

*At times the respondent Conferences before the Commission and their members will be referred to as the "respondent Conferences" or simply the "respondents".

"While we need not decide that this section (conferring the power to investigate) confers power to act to promote ports, *it is indicative of a congressional policy favoring port improvement and development. That policy having been expressed, the Board could, if it was not bound to do so, examine the practices here complained of in the light of that policy, and exercise its power to approve or disapprove such practices accordingly.* The Board did consider this policy in determining whether or not to approve equalization as practiced by the Conference. We must therefore conclude that the Board's orders here under attack were authorized and supported by statute." (246 F.(2d) 716. Emphasis supplied.)

In the Board's decision which the Court upheld, the Board, in finding that the equalization violated the principles and policies of Section 8 of the Merchant Marine Act, 1920, commented as follows with respect to that section:

"* * * That section requires, all other factors being substantially equal, that a given geographical area and its ports should receive the benefits of or be subject to the burdens naturally incident to its proximity to another geographical area. * * *"

"Section 8 charges the Board with the duty to promote and encourage the use by vessels of ports adequate to care for the freight which would naturally pass through such ports." (4 F.M.B. 679.)

Since the Court of Appeals held that Section 8 of the Merchant Marine Act, 1920, was properly applied to condemn the port equalization involved in that case because of the resulting diversion of cargo from the port equalized against, Section 8 should likewise be held to be applicable to condemn the port equalization in the case here under review.

Moreover, the Port of Stockton has been developed by the expenditure of \$23,000,000, of which \$17,300,000 represents Government funds, including \$3,800,000 of Federal funds. (Rep. Tr. 33, Phelps.) In view of Section 8 of the Merchant Marine Act, 1920, it was certainly never the intent of Congress that the welfare of a port—and especially a port developed with Government funds—should be left to the mercy of steamship lines, and even foreign steamship lines, cloaked with authority to divert cargo from such a port by the artificial device of rebates to shippers.*

By diverting cargo from the Port of Stockton to ports on San Francisco Bay, the port equalization here involved produces results directly opposite of promoting and encouraging the use by vessels of a port for freight which would naturally pass through that port—which is the policy expressed by Congress in Section 8. Such port equalization, therefore, results in a clear violation of the principles and policy of Section 8.

The port equalization rules here involved are set forth in the Conference tariffs and are consequently agreements between the member lines. Since such rules specify the circumstances in which the Conference members may apply port equalization, they regulate competition and are co-operative working arrangements between the members. They are therefore within the scope of Section 15 of the Shipping Act, 1916, (46 U.S.C. 814), and are subject to the provisions of that section.

Section 15 of the Shipping Act, 1916, provides that the Commission shall disapprove or cancel any agreement between common carriers by water that it finds “to be con-

*As recently as the year 1965 Congress approved a project for deepening and otherwise improving the waterways to Stockton which will involve the expenditure of approximately \$60,000,000. (Public Law 89-298.)

trary to the public interest". Congress has determined in Section 8 of the Merchant Marine Act, 1920, that the use of ports by vessels should be promoted and encouraged for the handling of freight that would naturally pass through such ports. The use of the Port of Stockton by vessels for the handling of cargo that would naturally pass through that port is therefore in the public interest.

Since they decrease and discourage the use of the Port of Stockton by vessels for handling such traffic, in violation of the Congressional policy specified in Section 8 of the Merchant Marine Act, 1920, such equalization rules and practices are, as a matter of law, contrary to the public interest, and the Commission should have ordered the rules cancelled from the Conference tariffs, on the ground that they are agreements between common carriers by water which are contrary to the public interest and hence in violation of Section 15 of the Shipping Act, 1916.

b. Disregard of Section 8 in Determining Public Interest.

The Commission likewise erred in failing to consider the Congressional policy expressed in Section 8 of the Merchant Marine Act, 1920, in its determination of whether the equalization rules and practices are "contrary to the public interest" under Section 15 of the Shipping Act, 1916.

In its Report the Commission concluded that port equalization against the Port of Stockton on cargo moving over a port on San Francisco Bay is not contrary to the public interest because, according to the Commission, it is beneficial to shippers and to the carriers which equalize against Stockton instead of sending their vessels to Stockton. (Com. Rep. 20-22, R. 1285-87.) In reaching this conclusion the Commission completely disregarded the interest of the Port of Stockton and of ocean carriers which serve or desire to serve Stockton.

The Commission found specifically that to eliminate equalization "would be beneficial to the Port of Stockton". (Com. Rep. 20, R. 1285.) In view of Section 8 of the Merchant Marine Act, 1920, (46 U.S.C. 867), the Commission erred in failing to give proper consideration to the interest of the Port of Stockton in determining whether the equalization rules and practices are contrary to the public interest and hence in violation of Section 15 of the Shipping Act, 1916.

In and by Section 8 of the Merchant Marine Act, 1920, Congress (as we have pointed out hereinabove) has determined that it is in the public interest to promote and encourage the use of ports by vessels for the handling of cargo that would naturally pass through such ports. This indicates that in determining what is in the public interest, not only should the interest of such a port—here Stockton—be considered, but also the interest of ocean carriers which serve or desire to serve Stockton by sending their vessels to that port.

The Commission has disregarded this policy laid down by Congress. It has determined wherein the public interest lies by considering only the interest of certain shippers and of ocean carriers who, by means of equalization, are able to defeat the desires of Congress by avoiding sending their vessels to Stockton and still handling cargo that would otherwise move over the Port of Stockton. As the dissenting opinion of Commissioner Hearn states,

"At least one conference carrier has provided substantial scheduled service at the Port of Stockton. The majority's action today will bless the efforts of those carriers who have no intention of giving direct service to the port, and those carriers who have traditionally bypassed the port, with the opportunity to drain its general cargo. * * *" (Com. Rep. 29, R. 1295.)

In determining the public interest under Section 15 of the Shipping Act, 1916, the Commission has thus disregarded the will of Congress, and has erred as a matter of law by basing its conclusion on improper factors and disregarding the factors that should properly be considered.

The Commission should have concluded that the equalization rules and practices are contrary to the public interest, in violation of Section 15 of the Shipping Act, 1916, because they are detrimental to the Port of Stockton and to ocean carriers which serve or desire to serve Stockton.

c. Impropriety of Disregarding Section 8 of Merchant Marine Act, 1920.

Perhaps brief comment should be made concerning the contention of our opponents that Section 8 of the Merchant Marine Act, 1920, should be disregarded because, they contend, the functions specified in such Section 8 were not specifically transferred to the Commission under Section 103 of Reorganization Plan No. 7 of 1961 (75 Stat. 840, 46 U.S.C.A. 1111 note), when the Federal Maritime Administration and the Federal Maritime Commission were separated.

Section 8 of the Merchant Marine Act, 1920, remained part of the law of the land, and the policy expressed therein continued to be the policy of Congress. Even if it were no longer required to make the investigations specified in Section 8, the Federal Maritime Commission cannot properly ignore the policy of Congress expressed in that section and—as it has done here—take action directly contrary to the Congressional policy expressed therein.

**VIOLATION OF SECTION 205 OF
MERCHANT MARINE ACT, 1936**

Section 205 of the Merchant Marine Act, 1936, (46 U.S.C. 1115), provides as follows:

“Without limiting the power and authority otherwise vested in the Commission, it shall be unlawful for any common carrier by water, either directly or indirectly, through the medium of an agreement, conference, association, understanding, or otherwise, to prevent or attempt to prevent any other such carrier from serving any port designed for the accommodation of ocean-going vessels located on any improvement project authorized by the Congress or through it by any other agency of the Federal Government, lying within the continental limits of the United States, at the same rates which it charges at the nearest port already regularly served by it.”

In its Report the Commission has found:

“* * * Stockton is a port designed for the accommodation of ocean-going vessels, located on an improvement authorized by the Congress, and is therefore entitled to the protection of Section 205, as our predecessor said of the Port of Stockton and other bay area ports in *Encinal Terminals v. Pacific Westbound Conference*, 5 F.M.B. 316, 320 (1957). * * *” (Com. Rep. 22, R. 1287.)

The Commission has also found

“* * * Although equalization is optional under the tariff, *carriers find that competition compels them to equalize.*” (Com. Rep. 8, R. 1273. Emphasis supplied.)

This means that a Conference carrier whose managerial judgment would lead it to serve the Port of Stockton by

sending its vessel to Stockton to load cargo, is compelled, in order to meet the competition of other Conference carriers, to refrain from sending its vessel to Stockton, and instead of serving Stockton, to load the cargo at another port, such as San Francisco, and rebate, through port equalization, the difference between the inland transportation charges to the port of loading and the lower inland transportation charges to Stockton.

By reason of the Conference equalization rule, and the practice of the Conference members thereunder, a carrier which would otherwise send its vessel to Stockton is prevented from serving Stockton because of the necessity of meeting the competition of other carriers which handle the cargo over San Francisco by means of port equalization.

The Conference equalization rule, and the action of the Conference carriers, have therefore prevented another common carrier by water from serving Stockton—in clear violation of Section 205 of the Merchant Marine Act, 1936, which is quoted immediately hereinabove.

The Commission should have concluded that the port equalization rules set forth in the Conference tariff pursuant to the agreement of the Conference carriers, and the actions of such carriers under those rules, are unlawful because they result in violations of Section 205 of the Merchant Marine Act, 1936.

Here, again, whether such Section 205 was specifically mentioned in Reorganization Plan No. 7 of 1961 (75 Stat. 840, 46 U.S.C.A. 1111 note) in connection with the functions transferred to the Commission is immaterial, since that section is part of the law of the land and the action of the Commission must be in conformity therewith.

UNLAWFUL REBATES RESULTING FROM THE EQUALIZATION RULES AND PRACTICES

Another ground of unlawfulness of the respondent Conferences' equalization rules and practices is that they result in unlawful rebates, in violation of Section 16 (Second) of the Shipping Act, 1916, (46 U.S.C. 815).

The Commission has found that some of the cargo which moved over San Francisco from an area where the inland transportation charges were lower to Stockton than to San Francisco, and on which the Conference carriers absorbed the difference between the inland transportation charges to Stockton and to San Francisco, would have moved over the Port of San Francisco without any such absorption of inland transportation charges. In this respect the Commission found:

(a) "If there were no equalization, many perishable commodities would still move through San Francisco rather than Stockton". (Com. Rep. 8, R. 1273.)

(b) "not all the equalized cargo would have gone to Stockton but for equalization". (Com. Rep. 14, R. 1279.)

These were instances where, for some special reason, such as using a particular steamship line or desiring the last port of loading, a shipper would have paid higher inland transportation charges to load his cargo at San Francisco without any port equalization payments by the ocean carrier.

In such a situation the payment by the ocean carrier of part of the shipper's inland transportation charges is a purely unnecessary gratuitous rebate.

Section 16 (Second) of the Shipping Act, 1916, which is quoted in Appendix B hereof, provides that it is unlawful for any common carrier by water to allow any person to

obtain transportation for property at less than the regular rates or charges of such carrier by any unjust or unfair device or means.

It has been held that the buying and furnishing of storage by an ocean carrier for its shipper or consignee at a port is an unlawful rebate, in violation of such Section 16 (Second). (*Investigation of Storage Practices of Pacific Far East Line, Inc., et al.*, 6 F.M.B. 301 (1961).) Similarly, the payment by the ocean carrier of part of the shipper's inland transportation charges to San Francisco when the shipper would have moved his cargo to San Francisco without such payment is an unlawful rebate, in violation of Section 16 (Second) of the Shipping Act, 1916.

The Commission therefore erred as a matter of law in failing to find that the equalization rules and practices are unlawful on this additional ground.

V.

UNFAIRNESS, UNJUST DISCRIMINATION AND UNDUE PREJUDICE AGAINST THE PORT OF STOCKTON

The majority of the Commission has taken an involved approach in reaching the conclusion that the equalization rules and practices on cargo loaded at a port on San Francisco Bay do not result in unjust discrimination or undue prejudice against the Port of Stockton. Consequently a somewhat extended reply is required in this connection.

Actually there are two very simple approaches which show readily that such equalization rules and practices are unfair, unjustly discriminatory and unduly prejudicial against the Port of Stockton, in violation of Sections 15 and 16 (First) of the Shipping Act, 1916, (46 U.S.C. 814, 815).

In the first place, as we have seen, by paying rebates of part of the inland transportation charges to a San Francisco Bay port, the Conference carriers have diverted cargo from the Port of Stockton and have decreased and discouraged the use of the Port of Stockton by vessels for the handling of cargo. We have also seen that this is directly in violation of the policy of Congress expressed in Section 8 of the Merchant Marine Act, 1920—namely, the policy of encouraging the use by vessels of ports for the handling of cargo that would naturally pass through such ports. The Conference carriers discriminate against, and prejudice, the Port of Stockton by rebating part of the inland transportation charges on cargo shipped to San Francisco, and not making a similar rebate if the cargo is moved to Stockton. Discrimination and prejudice which result in a direct violation of an expressed Congressional policy to the contrary must be held to be “unjust” and “undue” as a matter of law.

In the second place, it should be noted that the second paragraph of Section 15 of the Shipping Act, 1916, provides that the Commission shall cancel or modify any agreement “that it finds to be unjustly discriminatory *or unfair* as between * * * ports”. How can it possibly be said that a rebating device which diverts from the Port of Stockton to a San Francisco Bay port cargo which would otherwise move over the Port of Stockton is *fair* to that port? The record obviously will not support a finding that the port equalization under consideration is not “unfair” to the Port of Stockton. The Commission erred in not finding that such port equalization is unfair to the Port of Stockton and in not requiring the cancellation of the equalization rules.

But instead of applying these easy approaches which show clearly unfairness, unjust discrimination and undue prejudice against the Port of Stockton, the Commission has adopted a more complicated approach to this question, which will be discussed next.

The Commission concluded that the respondents' equalization rules which permit equalization against the Port of Stockton on cargo loaded at the Ports of Los Angeles and Long Beach are unjustly discriminatory and unfair between ports within the meaning of Section 15 of the Shipping Act, 1916.* (Com. Rep. 25-27A, R. 1290-93.)

The two grounds specified by the Commission for reaching a different conclusion for equalization against Stockton on cargo loaded at a San Francisco Bay port will be considered separately.

a. "Bay Area" Ports and "Geographical Area".

The Commission first finds a distinction between cargo loaded at Los Angeles and Long Beach and cargo loaded at San Francisco because, according to the Commission, Stockton and San Francisco are both San Francisco "bay area" ports and are hence both in the same "geographical area". (Com. Rep. 12, R. 1277.)

In his dissenting opinion, Commissioner Hearn has taken violent exception to this attempted distinction between the loading of cargo at Los Angeles and at San Francisco. Commissioner Hearn has correctly declared that Stockton "can in no way be considered a San Francisco Bay area port". (Com. Rep. 27A, R. 1293.) With respect to these distinguishing findings of the majority of the Commission, Commissioner Hearn has stated:

*Section 15 is applicable because the equalization rules are contained in the Conference tariffs, which constitute agreements between common carriers by water which are subject to Section 15.

"In reaching its ultimate conclusion, the majority found that (1) the port of Stockton is a port in the San Francisco Bay area, and (2) cargoes naturally tributary to Stockton are also naturally tributary to San Francisco. While I think neither of these findings is correct, I believe they skirt and confuse the central issue, which is: Do these tariff rules result in an unjust discrimination to the port of Stockton? The findings, moreover, are not supported by the facts, and have no valid basis in law.

First, the port of Stockton is not a San Francisco Bay port within the meaning of any statute administered by this Commission, and the cited 'comprehensive report' of the California Legislature in 1951 referring to Stockton as a Bay Area port certainly is not controlling here, if indeed it has any relevance at all. The incontrovertible facts are that Stockton is some 107 constructive miles and several distinct waterways moved from San Francisco Bay. It is unthinkable that the Port of Stockton should be considered as juxtaposed to San Francisco, Oakland, Alameda and Richmond. The finding that Stockton should be treated as a San Francisco Bay port must hang as an unwarranted fiction upon which no legal conclusion can be based.

Secondly, to say, as does the majority, that the 'natural direction of the flow of traffic from the San Joaquin Valley . . . is through the Golden Gate to the Pacific Ocean' begs the question. The point at issue is whether the 'natural direction of the flow of traffic from the San Joaquin Valley . . . through the Golden Gate . . .' is through San Francisco or through Stockton. I hold to the belief that this natural flow is through Stockton, and succinctly stated, but for the equalization, an admittedly artificial device, San Joaquin exports would normally flow through the Golden Gate via Stockton, except where, *for the convenience of the cargo*, shippers are not only willing to but should pay

their fair share of costs of the premium service offered at San Francisco." (Com. Rep. 30-31, R. 1296-97.)

The only support indicated by the majority of the Commission for its finding that Stockton and San Francisco are both San Francisco "bay area" ports and are hence both in the same "geographical area" is twofold—first, that "the California Legislature in a comprehensive report on the San Francisco ports issued in 1951 consistently referred to Stockton as a Bay area port" (Com. Rep. 12, R. 1277); and second, that "In setting up the Bay Area Protection and Promotion Program, now contained in *Harbors and Navigation Code*, section 1980, et seq., the San Francisco Bay Area is defined by the California Legislature as—

' . . . that region served by commercial shipping and transportation passing through the Golden Gate, including tributary areas of central and northern California . . . ' " (Com. Rep. 12, R. 1277.)

Obviously, the California Legislature was using the term "San Francisco Bay Area" merely as a term of convenience. The Legislature was not attempting to transpose the San Joaquin Valley, in which Stockton is located, to San Francisco Bay—which of course it could not do by legislative fiat. That the Legislature was merely using a term of convenience is clear from the introductory portion of Section 1980 of the *California Harbors and Navigation Code*, which was omitted in the Commission's Report and which states:

"As used in this article, the 'San Francisco Bay area' means that region served" etc. (Emphasis supplied.)

That this definition of the San Francisco Bay Area is meaningless is apparent from the fact that if anything

moved from Red Bluff, in the upper Sacramento Valley, down the Sacramento River, Red Bluff would be considered part of the San Francisco Bay area—which of course is absurd.

Actually, neither the report of the California Legislature nor the California statute constitutes “*evidence*” showing that, as a matter of *fact*, Stockton is part of the San Francisco Bay Area. Moreover, neither the legislative report nor the California statute was offered in evidence in this proceeding, and neither is part of the record on which the Commission’s decision could be based. Section 7 (d) of the Administrative Procedure Act (5 U.S.C. 1006) provides:

“The transcript of testimony and exhibits, together with all papers and requests filed in the proceeding, shall constitute the exclusive record for decision * * *.”

Certainly the Legislative Report and the statute cited by the Commission cannot change the fact that Stockton is located in the San Joaquin Valley, 84 miles by water from San Francisco (Rep. Tr. 30, Phelps.) and five waterways removed from San Francisco Bay—by San Pablo Bay, Carquinez Strait, Suisun Bay, the San Joaquin River, and the Stockton Deep Water Channel (Ex. 7).

Since the Commission’s finding that Stockton and San Francisco are in the same “geographical area” is based on its finding that both are in the San Francisco Bay area, the finding with respect to the same “geographical area” is likewise unsupported by any evidence. It is well known that Stockton is in the San Joaquin Valley, which is an entirely distinct area from that surrounding San Francisco Bay. This is apparent from the map in evidence as Exhibit No. 4, and especially the relief map in the lower left hand corner of that exhibit, which shows how completely the San Joaquin Valley is separated from San Francisco Bay geographically.

Cargo loaded at San Francisco or any other port located on San Francisco Bay cannot properly be treated differently from cargo loaded at Los Angeles or Long Beach by declaring that Stockton and San Francisco are both "bay area" ports and are both in the same "geographical area".

b. "Naturally" Tributary Territory.

The second ground on which the Commission distinguishes cargo loaded at San Francisco and other San Francisco Bay ports from cargo loaded at Los Angeles and Long Beach is that the territory which is "naturally" tributary to Stockton is also "naturally" tributary to San Francisco and other ports on San Francisco Bay. (Com. Rep. 16, R. 1281.)

In reaching this conclusion the Commission has completely overlooked the meaning and application of port equalization, and the provisions of the Conference equalization rules here involved. Under the principles of port equalization and the terms of such rules, it is impossible to have an area "naturally tributary" to two different ports in a situation where port equalization is applied.

The very function and purpose of port equalization is to prevent cargo from moving over a port *over which it would otherwise move*, and to load it over another port to which the inland transportation charges are higher than to the port over which the cargo would otherwise move. If the cargo would move over the more distant port at which it was actually loaded without the absorption by the ocean carrier of the additional inland transportation charges, *then there would be no need or justification for port equalization on such cargo. This is recognized by the Conference equalization rules here involved, which limit the application of port equalization to the following situation:*

“* * * cargo which would normally move from one California terminal port, may be shipped under equalization via another California terminal port.”* (See paragraph (e) of Appendix A hereto.) (Emphasis supplied.)

The Conference equalization rules themselves, therefore, limit the making of port equalization payments to situations where otherwise the cargo would normally move over another port. Relating this to the ports of Stockton and San Francisco, this means that port equalization payments on cargo loaded at San Francisco can only be made in instances where without such equalization payments the cargo “would normally move” over the Port of Stockton. Obviously, if the cargo would otherwise normally move over the Port of Stockton, this shows that such cargo is “naturally tributary” to the Port of Stockton. If in the absence of port equalization payments it would normally move over the Port of Stockton, such cargo cannot also be “naturally tributary” to San Francisco.

The result, therefore, is that on all cargo loaded at San Francisco on which port equalization is permitted under the Conference rules, all of such cargo would otherwise normally move over the Port of Stockton, and hence is “naturally tributary” to Stockton, and not to San Francisco. The area from which such cargo moves, therefore, is “naturally tributary” to Stockton and not to San Francisco.

Actually, the record shows that cargo from the entire San Joaquin Valley in California would normally move over the

*Rule No. 5 of the Pacific Westbound Conference Tariff shows that the following ports in California are terminal ports in that Conference: San Diego, Los Angeles Harbor, Long Beach, San Francisco, Alameda, Oakland, Richmond, Stockton and Sacramento. (Ex. 1-C.) The terminal ports in California are the same in the Pacific Straits and Pacific/Indonesian Conferences, except that Sacramento is not a terminal port in those Conferences. (Ex. 2-A, 3-A.)

Port of Stockton in the absence of port equalization because the inland transportation charges are lower from that area to the Port of Stockton than to any other port (Rep. Tr. 731, Rollins; Ex. 4, 10, 30, 32, 33, 34). The San Joaquin Valley area, therefore, is "naturally tributary" to the Port of Stockton, and not to San Francisco or any other port located on San Francisco Bay.

The Commission has completely overlooked the fact that under the Conference rules themselves, in no instance where port equalization is permitted can such cargo be "naturally tributary" to more than one port—namely, the port over which it would normally have moved in the absence of such equalization. *The Commission's finding that the area which is "naturally tributary" to the Port of Stockton is also "naturally tributary" to San Francisco is therefore directly contrary to the Conferences' own rules and wholly without support in the record.*

To the extent that any cargo on which the inland transportation charges are lower to Stockton than to San Francisco would move via San Francisco without the port equalization payments, the movement via San Francisco would be for some peculiar reason of the shipper, such as the desire of the consignee for the use of a particular vessel that did not call at Stockton, and it could not be said to be a "natural" movement or to make the area "naturally tributary" to San Francisco. Actually in such a situation the making of port equalization payments would be improper under the Conference rules because the cargo would not "normally move" over the Port of Stockton. Moreover, as we have seen, the making of a port equalization payment in such a situation would be a clear rebate because the cargo would have moved over San Francisco without such payment, and the equalization payment is a pure gratuity to the shipper of part of the transportation charges that he would otherwise pay.

On what does the Commission rely in support of its finding that the territory which is naturally tributary to Stockton is also naturally tributary to San Francisco?

First, that the natural flow of traffic from the San Joaquin Valley is through the Golden Gate. (Com. Rep. 13, R. 1278.) As Commissioner Hearn has pointed out in the portion of his dissenting opinion which is quoted hereinabove, this does not show whether the "natural flow" is over the Port of Stockton or over the Port of San Francisco, which is the question.

Second, the Commission states that before Stockton became accessible to oceangoing vessels, San Francisco was the principal port for San Joaquin Valley freight and it did not cease to be such a port merely upon the creation of an additional port at Stockton. (Com. Rep. 13, R. 1278.) This statement is entirely unsupported by, and directly contrary to, the record and other findings of the Commission. The Conference rules make port equalization applicable only when such cargo would otherwise normally move over the Port of Stockton. As pointed out hereinabove, the record shows that cargo from the San Joaquin Valley would normally move over the Port of Stockton because of lower inland transportation charges to that port. The fact is that San Francisco's picture changed when cargo from the San Joaquin Valley could move over the Port of Stockton. Thereafter the movement of most of such cargo could be forced over the Port of San Francisco only by means of the equalization payments. This completely refutes the Commission's finding that the San Joaquin Valley is "naturally tributary" to San Francisco, as well as to Stockton.

Finally, in finding that the territory which is "naturally tributary" to Stockton is also "naturally tributary" to San Francisco, the Commission refers to a publication of the

Maritime Administration and the Army Engineers which purports to describe the "Tributary Territory" of various ports, the "Tributary Territory" described for Stockton being within that described for San Francisco and certain other San Francisco Bay ports. (Com. Rep. 15-16, R. 1280-81.) The publication cited by the Commission does not purport to describe the "naturally" tributary territory of the respective ports in the sense of the territory from which cargo would *normally move* over a particular port. Such publication merely refers to the territory from which the respective ports obtain some of their traffic. The fact that some shippers would be willing to pay a premium in inland transportation charges to reach a more distant port, for some reason peculiar to such shipper, does not show that the territory is "naturally" tributary to the more distant port. That the term "naturally tributary" territory has been used in port equalization decisions as meaning the area from which the inland transportation rates and the distances are lower to a particular port than to any other port is apparent from the following language in the case of *City of Portland v. Pacific Westbound Conference*, 4 F.M.B. 664:

"* * * cargoes on which absorptions of inland freight charges are made originate in areas naturally and geographically tributary to Northwest points *because of inland transportation rates favorable to those ports as well as through closer proximity* * * *." (Page 675. Emphasis supplied.)

The term "tributary territory" was certainly not used in this sense in the publication cited by the Commission. The record shows that from the San Joaquin Valley area the inland transportation rates and the distances are less to Stockton than to San Francisco. (Rep. Tr. 731, Rollins; Ex. 4, 10, 30, 32, 33, 34.) Applying the test of "naturally

tributary" specified in the *City of Portland* case, *supra*, therefore, the San Joaquin Valley area—which is "naturally tributary" to Stockton—cannot possibly also be "naturally tributary" to San Francisco. The Commission's finding to the contrary is unsupported by substantial evidence.

In connection with its finding that the territory naturally tributary to Stockton is also naturally tributary to San Francisco, the Commission adds that "the territory surrounding Stockton and the entire Bay area is centrally, economically and naturally served by the conference facilities at San Francisco". (Com. Rep. 16, R. 1281.) This merely begs the question, which is whether the territory surrounding Stockton and the San Joaquin Valley may *lawfully* be served by the conference facilities at San Francisco by means of port equalization. Moreover, as we have pointed out, serving the San Joaquin Valley through San Francisco by means of port equalization cannot possibly be said to be serving it "naturally", and there is no evidence in the record to support such a finding.

Summarizing briefly, the Commission has endeavored to distinguish cargo loaded at Los Angeles and Long Beach from cargo loaded at San Francisco or any other port on San Francisco Bay on the grounds that Stockton and San Francisco are both in the San Francisco "bay area" and hence both in the same "geographical area", and that the territory which is "naturally tributary" to Stockton is also "naturally tributary" to San Francisco. We have seen that neither of these grounds is supported by substantial evidence in this proceeding. The Commission concluded that port equalization against Stockton on cargo loaded at Los Angeles and Long Beach was unlawful because it diverted from Stockton cargo that would otherwise move over that port. Since port equalization on cargo loaded at San Francisco or any other port on San Francisco Bay diverts from

Stockton cargo that would otherwise move over that port, the Commission should likewise have held that port equalization against Stockton on cargo moving over a port on San Francisco Bay is unlawful.

Actually, however, for a determination of whether the port equalization in question is unlawful, it is wholly immaterial whether Stockton and San Francisco are said to be both in the same "geographical area", and whether the territory which is "naturally tributary" to Stockton is said to be also "naturally tributary" to San Francisco. This aspect will be considered next.

c. Immateriality of Same "Geographical Area" and Same "Naturally Tributary Territory".

The term "geographical area" has no precise limitations. There are varying degrees of geographical areas. It is possible to consider as a single "geographical area" all of California north of the Tehachapi Mountains, or even all of California, the entire Pacific Coast, or the Pacific Slope west of the Rocky Mountains. Consequently, to say that Stockton and San Francisco are in the same "geographical area" is meaningless with respect to the issue in this proceeding.

Similarly, the term "naturally tributary" territory can be used with different meanings. We have pointed out that in its Report here involved, the Commission has not used that term in accordance with its meaning in other port equalization decisions.

This case cannot be decided properly on the basis of meaningless terminology. It must be decided on the basis of applicable principles of law, which the Commission did not do. A difference in mileage from the origin of the cargo to the loading port (from Fresno to Los Angeles versus to San Francisco) obviously does not justify the application

of different principles of law in connection with port equalization against the Port of Stockton.

In order to determine whether respondents' port equalization on cargo loaded at San Francisco or any other port on San Francisco Bay results in unjust discrimination and undue prejudice against the Port of Stockton, in violation of Sections 15 and 16 (First) of the Shipping Act, 1916, it is necessary to determine whether such port equalization diverts from Stockton cargo which would otherwise move over that port. This principle has been stated briefly as follows by the Commission's predecessor in *City of Mobile v. Baltimore Insular Line, Inc.*, 2 U.S.M.C. 474 (1941):

"To permit continuation of unrestricted solicitation by carriers for business through condonation of a practice whereby unfavorable inland rates are overcome would wholly ignore the right of a port to traffic to which it may be entitled by reason of its geographical location. Such right appears fundamental under statutes designed to establish and maintain ports. * * *"
(Page 486.)*

The same principle was followed in *Beaumont Port Commission v. Seatrains Lines, Inc.*, 3 F.M.B. 556 (1951), wherein the following conclusion was reached:

"* * * We find that a drawing away of traffic from the Gulf ports results in undue prejudice and is due to the individual act of respondent in establishing its equalization practice. * * *"
(Page 566.)

In the case of *City of Portland v. Pacific Westbound Conference*, 4 F.M.B. 664 (1955), the Federal Maritime Board found the equalization rule and practices of the Pacific Westbound Conference to be unjustly discriminatory and unfair between ports within the meaning of Section 15 of

*This quotation was cited and followed as recently as 1960 in *Proportional Rates on Cigarettes and Tobacco*, 6 F.M.B. 48 (1960).

the Shipping Act, 1916, on the basis of evidence which it summarized as follows:

"In support of their allegations of discrimination and preference, the complaining ports have adduced evidence showing or tending to show that (a) competition exists between Pacific Northwest ports and the port of San Francisco for the same commodities; (b) diversions of traffic are effected by conference carriers through absorptions of inland transportation charges on shipments from San Francisco on cargo originating in Northwest producing areas; (c) cargoes on which absorptions of inland freight charges are made originate in areas naturally and geographically tributary to Northwest points because of inland transportation rates favorable to those ports as well as through closer proximity; and (d) the conference equalization rule has proximately caused a substantial loss of cargo to Northwest ports." (Pages 674-675.)

In the *City of Portland* case, *supra*, the Board also declared:

"* * * To the extent, therefore, that the ports of a given geographical area give or can give adequate transportation services, we look with disfavor on equalization rules or practices which divert traffic away from the natural direction of the flow of traffic." (Page 679.)

The Port of Stockton is an entirely separate and independent port, and is entitled to have these principles applied to it regardless of whether, as a result of the rebating of inland transportation charges, the cargo is loaded on the ocean vessel at Los Angeles or San Francisco.

The respondent Conferences have themselves recognized that the Port of Stockton is an entirely separate and distinct port. Their tariffs name Stockton as a "terminal port" entirely separate and distinct from ports located on San Francisco Bay which are designated "terminal ports". (Ex.

1-C, 2-A, 3-A.) A "terminal port" is a port from which the regular Conference freight rates apply without restriction.

In various cases before them, the Commission's predecessors have also recognized Stockton as a port entirely separate and distinct from ports on San Francisco Bay. See, for example, *Sun-Maid Raisin Growers Association v. Blue Star Line, Ltd.*, 2 U.S.M.C. 31 (1939), and *Encinal Terminals et al. v. Pacific Westbound Conference et al.*, 5 F.M.B. 316 (1957). As a matter of fact, in both of those cases the Conferences and even the Port of San Francisco argued that the Port of Stockton was so completely separate and distinct from the Port of San Francisco that different rates and rules should apply at Stockton from what applied at San Francisco.

It should be noted how completely the evidence in this case with respect to cargo equalized against Stockton and loaded at San Francisco resembles the evidence in the *City of Portland* case, *supra*, on the basis of which the Federal Maritime Board held that the port equalization there involved was unjustly discriminatory between ports and hence unlawful. (See the quotation from the *City of Portland* case on page 39, *supra*.) Here the Commission's Report shows that (a) competition exists between Stockton and San Francisco for the same commodities; (b) diversions of traffic are effected by Conference carriers through absorptions of inland transportation charges on shipments from San Francisco on cargo originating in the San Joaquin Valley; (c) such cargoes originate in an area naturally and geographically tributary to the Port of Stockton because of inland transportation rates favorable to Stockton, as well as through closer proximity to Stockton; and (d) the Conference equalization rules have proximately caused a substantial loss of cargo to the Port of Stockton.

The conclusion of the Board in the *City of Portland* case that under these circumstances the port equalization was

unjustly discriminatory and unduly prejudicial between ports was affirmed by the United States Court of Appeals in the case of *Pacific Far East Line v. United States*, 246 F.(2d) 711 (C.A., D.C. 1957). The Port of Stockton is entitled to have a similar holding in this case on the basis of such evidence—namely, that port equalization against Stockton on cargo loaded at San Francisco or any other port on San Francisco Bay is unjustly discriminatory and unduly prejudicial between ports and hence unlawful, in violation of Sections 15 and 16 (First) of the Shipping Act, 1916.

Perhaps a brief comment should be made with respect to the language of the *City of Portland* case concerning adequacy of service at the port equalized against. In our case the Commission has not made any finding that port equalization on cargo loaded at San Francisco is justified by inadequacy of service at Stockton. Consequently, such equalization cannot be justified on the ground of inadequacy of service at Stockton. Actually, inadequacy of service at Stockton could not be a proper ground of justification of the equalization, because any inadequacy of service at Stockton would result directly from the action of the Conference members in refusing to serve Stockton, and could not properly be charged against the Port of Stockton.

On what, then, does the Commission attempt to justify reaching a different conclusion in our case on evidence similar to that on which unjust discrimination was found in the *City of Portland* case? On the basis of the decision of the former Maritime Commission in *Beaumont Port Commission v. Seatrains Lines, Inc.*, 2 U.S.M.C. 699 (1943). (Com. Rep. 12-13, 15, R. 1277-78, 1280.) In that case the Commission's predecessor permitted equalization against Houston and Galveston, Texas, on cargo loaded by Seatrains Lines at Texas City, but it held that equalization of Texas

City with Beaumont, Texas, by absorption of inland transportation charges was unlawful. The Commission's predecessor found that in a geographical sense Texas City, Galveston and Houston "may be described as Galveston Bay ports" (page 702), but that "Beaumont is an inland port" (page 702).

Because the Commission concluded that Stockton and San Francisco are both "bay area" ports and hence in the same "geographical area", it held that the *Beaumont* case indicated that port equalization was proper between Stockton and San Francisco just as it had been permitted in the case of Texas City, Galveston and Houston. This conclusion is improper because, as we have seen, Stockton and San Francisco are not both in the same geographical area. Actually, Stockton occupies a position similar to Beaumont—both being inland ports—and consequently a proper application of the *Beaumont* case leads to the conclusion that equalization between San Francisco and Stockton is unlawful.

Moreover, certain unique facts in the *Beaumont* case make that decision valueless as a matter of general principle. In the first place, the carrier involved there—Seatrains Lines—transported railroad freight cars on its vessels and it could not load the railroad cars on its vessels at an ordinary pier, but required special expensive facilities. The handling of this traffic over Texas City, where the required special facilities existed, avoided the necessity of constructing expensive facilities at Galveston and Houston. There is no such element involved in our case, since the freight here involved can be loaded over the regular docks of a port.

Also, another distinguishing feature of the *Beaumont* case was that no discrimination or injury could be shown from Seatrain's port equalization practice since Galveston

and Houston were not in a position to handle the Seatrain traffic because they lacked the special facilities required. In this connection the Commission said in the *Beaumont* case, referring to Galveston and Houston:

“* * * The owners of wharf facilities at these ports will lose revenue as a result of the use of Seatrain’s facilities, but that loss would be suffered even if Seatrain operated from Galveston and Houston, because none of the wharfingers there provides the peculiar facilities required by Seatrain’s operations.” (2 U.S. M.C. 703.)

Our situation is completely different with respect to the matter of discrimination, since, as we have seen, the equalization practices here involved deprive the Port of Stockton of cargo and revenue that it would otherwise receive. Consequently, the equalization rules and practices in our case result in discrimination in fact against Stockton—which was not true with respect to Galveston and Houston in the *Beaumont* case.

The *Beaumont* case, therefore, cannot properly be said to show that the equalization rules and practices here involved are not unjustly discriminatory against Stockton on cargo that is equalized over San Francisco. Such practices interfere with the normal movement of cargo over the port to which the inland rates are the lowest from the point of origin of the cargo. Stockton is entitled to be treated as a separate and distinct port. The principle of the other equalization cases cited hereinabove, and of the *Beaumont* decision with respect to Beaumont, is applicable in our case—namely, that port equalization which interferes with the normal movement of cargo results in unjust discrimination between ports and is unlawful.

Commissioner Hearn has set forth the correct principles of law which should be applied in determining whether the

port equalization here involved results in unjust discrimination and undue prejudice against the Port of Stockton on cargo loaded at San Francisco or any other port on San Francisco Bay. In his dissenting opinion he says:

"The only valid test, in this case, for determining whether or not the effectuation of the equalization rule, and consequently for determining whether respondents are giving 'any undue or unreasonable preference or advantage to any particular person, locality, or description of traffic' or subjecting 'any particular person, locality, or description of traffic to any undue or unreasonable prejudice or disadvantage' in violation of Section 16 First, is whether the traffic would move via San Francisco *but for* the equalization. Here, certainly, most of it *would not* and to the extent that the artificial device draws traffic from Stockton it is unlawful.

In this vein, I am convinced that the precedents support my view. There can be no doubt here that the equalized cargoes originate in areas 'naturally and geographically tributary (to Stockton) because of inland transportation rates favorable to (Stockton) as well as through closer proximity'. *City of Portland v. Pacific Westbound Conference*, 4 F.M.B. 664 (1955). Similarly, what was said in *City of Mobile v. Baltimore Insular Line, Inc.*, 2 U.S.M.C. 474 (1941), is appropriate here:

"To permit continuation of unrestricted solicitation by carriers for business through condonation of a practice whereby unfavorable inland rates are overcome would wholly ignore the right of a port to traffic which it may be entitled by reason of its geographical location. Such right appears fundamental under statutes designed to establish and maintain ports'.

Again, in the *Portland* case, *supra*, our predecessors interpreted section 8 of the Merchant Marine Act, 1920, as requiring:

'... that a given geographical area and its ports should receive the benefits of or be subject to the burdens naturally incident to its proximity or lack of proximity to another geographical area'.

Moreover, the second *Beaumont* case at 2 U.S.M.C. 699 (1943), so heavily relied upon by the majority, is inappropriate here. * * * (Com. Rep. 32-33, R. 1298-99.)

The Commission's conclusion that the equalization rules and practices here involved are not unjustly discriminatory or unduly prejudicial against the Port of Stockton on cargo loaded at San Francisco or any other port on San Francisco Bay is based on findings which are unsupported by substantial evidence, a misapplication of the *Beaumont* case, and the failure to apply the correct principles of law.

VI.

REMOVAL OF LANGUAGE "WHICH WOULD NORMALLY MOVE" FROM EQUALIZATION RULE

We have pointed out that the port equalization rule of each of the three Conferences here involved permits equalization over a California terminal port only with respect to "cargo which would normally move" over another California terminal port. (See paragraph (e) of Appendix A of this Brief.) This means that cargo can be equalized against the Port of Stockton and loaded over the Port of San Francisco only if without the equalization it would normally move over the Port of Stockton.

The Commission concludes in its Report that the language "which would normally move" should be removed from the equalization rule (Com. Rep. 23, R. 1288), and it so orders in its Order under consideration (R. 1301, 1305). The result of this is that a Conference carrier may, and does, load cargo at San Francisco on which it rebates to the shipper

the difference between his inland transportation charges to San Francisco and to Stockton even though the cargo would have moved over San Francisco without such payment of inland transportation charges by the ocean carrier. It will be recalled that the Commission found that there is such cargo—more specifically the Commission found that “If there were no equalization, many perishable commodities would still move through San Francisco rather than Stockton” (Com. Rep. 8, R. 1273), and that “not all the equalized cargo would have gone to Stockton but for equalization” (Com. Rep. 14, R. 1279).

As we pointed out in Section IV of our argument hereinabove, the payment to a shipper by an ocean carrier of the difference between the shipper’s higher inland transportation charges to San Francisco and his lower charges to Stockton is clearly an unnecessary gratuitous rebate, in violation of Section 16 (Second) of the Shipping Act, 1916, when the shipper would have paid the higher inland charges to move the cargo via San Francisco without such payment of part of the inland transportation charges by the ocean carrier.

The Commission’s conclusion that the language of the Conference rule restricting equalization to cargo “which would normally move” over a particular port should be eliminated from the rule is a wholly unwarranted attempt to read a clear restriction out of the rule on the basis of an entirely unsupported assumption that something other than the clear meaning was intended. In this connection the Commission said with respect to the restriction of the operation of the equalization rule to cargo “which would normally move” over another port:

“* * * This apparent restriction has no practical relation to the theory or operation of the rule. Perhaps

it was originally intended to make it clear that cargo may be equalized even though it might 'normally' move from another port, thus anticipating any objection on that ground. The rule should be drafted to exclude what is clearly not intended as a restriction. * * * (Com. Rep. 23, R. 1288.)

There is no support in the record for the Commission's finding that the language "which would normally move" was not intended as a restriction. Moreover, the statements quoted immediately hereinabove show a clear abuse of discretion and a complete lack of comprehension of port equalization by the Commission. Unless certain cargo would normally move over another port, such as Stockton, there would be absolutely no excuse or justification for the absorption by an ocean carrier of the difference between the shipper's inland transportation charges to such port and to a more distant port, such as San Francisco, over which the cargo would have moved without such absorption.

The Commission's interpretation of the Conference tariffs with respect to the restriction "which would normally move" over certain ports is clearly erroneous. Where, as here, the words of a tariff are used in their ordinary sense, the construction of the tariff presents solely a question of law which should be decided by the courts. (*Great Northern Railway Company v. Merchants Elevator Company*, 259 U.S. 285, 66 L. Ed. 943, 42 Sup. Ct. 477.) The Court should therefore construe the tariff on the basis of the language used therein, and should require that this restriction be given effect in accordance with its clear terms.

The Commission committed a serious error in ordering that the language "which would normally move" should be eliminated from the rule. Instead, the Commission should have admonished the respondents in the proceeding before

the Commission that, as the rule clearly specifies, port equalization should be applied only in instances where the cargo would normally move over another port.

VII.

VIOLATION OF FIFTH AMENDMENT

For the reasons which are explained in our discussion set forth hereinabove, the Commission's order unlawfully permits the Conference carriers to divert from the Port of Stockton, by means of port equalization against that port, cargo that would otherwise move over the Port of Stockton, resulting in the loss by that port of revenue that would otherwise accrue to it from terminal charges for handling the cargo.

By failing to prohibit such unlawful port equalization and permitting such diversion of cargo from the Port of Stockton, the Commission's order deprives petitioner Stockton Port District of property without due process of law, in violation of the Fifth Amendment to the Constitution of the United States.

VIII.

SUMMARY OF GROUNDS OF REVERSIBLE ERROR

This Court is charged with the duty of holding unlawful, and setting aside, an order of an administrative agency such as the Federal Maritime Commission, if the order is (1) based on findings which are unsupported by substantial evidence, (2) based on an error of law, (3) unsupported by adequate findings, or (4) arbitrary or an abuse of the agency's discretion or power. (Administrative Procedure Act, Section 10(e), (5 U.S.C. 1009); *Interstate Commerce Commission v. Louisville & Nashville Railroad Company*, 227 U.S. 88, 57 L. Ed. 431, 33 Sup. Ct. 185; *Universal Cam-*

era Corporation v. Board, 340 U.S. 474, 95 L. Ed. 456, 71 Sup. Ct. 456; *Morgan v. United States*, 298 U.S. 468, 80 L. Ed. 1288, 56 Sup. Ct. 906; *Interstate Commerce Commission v. Mechling*, 330 U.S. 567, 91 L. Ed. 1102, 67 Sup. Ct. 894; *Interstate Commerce Commission v. James McWilliams Blue Line, Inc.*, 100 F. Supp. 66, 342 U.S. 951, 96 L. Ed. 707, 72 Sup. Ct. 624; *Mitchell v. United States*, 313 U.S. 80, 85 L. Ed. 1201, 61 Sup. Ct. 873; *Henderson v. United States*, 339 U.S. 816, 94 L. Ed. 943, 42 Sup. Ct. 477.) Upon review, the Court is likewise required to "decide all relevant questions of law, interpret constitutional and statutory provisions". (Administration Procedure Act, Section 10(e), 5 U.S.C. 1009.)

The Commission's Order here under consideration is erroneous on all of the grounds hereinabove specified.

In attempting to distinguish the legal effect of equalized cargo loaded at Los Angeles and Long Beach, and at San Francisco and other San Francisco Bay ports, the Commission has relied on findings pertaining to the "same geographical area" and "naturally tributary territory" which are unsupported by substantial evidence. The Commission's conclusion that the language "which would normally move" should be eliminated from the equalization rule is likewise based on findings which are unsupported by substantial evidence.

The Commission's Order is based on errors of law in that the Commission applied erroneous and improper principles of law in concluding that port equalization against the Port of Stockton on cargo loaded at San Francisco or any other port located on San Francisco Bay (1) does not violate the policy of Section 8 of the Merchant Marine Act, 1920, (2) is not contrary to the public interest, in violation of Section 15 of the Shipping Act, 1916, (3) does not violate Section 205 of the Merchant Marine Act, 1936, (4) does

not result in unlawful rebates, in violation of Section 16 (Second) of the Shipping Act, 1916, and (5) does not result in unfairness, unjust discrimination and undue prejudice against the Port of Stockton. The Commission's Order directing that the language "which would normally move" be eliminated from the equalization rules is likewise based on errors of law.

The Commission's conclusions distinguishing between cargo loaded at Los Angeles and Long Beach and at San Francisco and other ports on San Francisco Bay, and its conclusion of lack of unjust discrimination and undue prejudice against the Port of Stockton, are unsupported by adequate findings.

The Commission's Order also deprives petitioner of its property without due process of law, in violation of the Fifth Amendment to the Constitution of the United States.

The conclusions of the Commission on each of the points hereinabove mentioned are arbitrary and an abuse of the Commission's discretion and power.

In his dissenting opinion, Commissioner Hearn has appraised the conclusions of the majority as follows:

"I disagree, however, with the results reached by the majority and am convinced that the subject equalization rules against Stockton are violative of Section 16 (First) of the Shipping Act, contrary to the public interest standard of Section 15, and in contravention of the principles and policies of Section 8 of the Merchant Marine Act, 1920, and Section 205 of the Merchant Marine Act, 1936.

I read the majority's action today as (1) frustrating the will of Congress in developing new and modern ports and (2) turning over to conference carriers, the right to determine which of our ports shall prosper and which shall suffer. * * *" (Com. Rep. 27A-28, R. 1293-94.)

We commend Commissioner Hearn's dissenting opinion (Com. Rep. 27A-33, R. 1293-99) to the Court for a correct statement of the principles of law on various points which the majority of the Commission decided erroneously.

IX.

CONCLUSION

The power to determine which ports in the United States shall prosper and which shall have cargo that would otherwise move over them diverted to other ports should not be placed in the hands of conference carriers, and even foreign steamship lines. Surely artificial devices in the form of rebates of part of the inland transportation charges should not be sanctioned to divert cargo from its normal course—especially in the face of the expressed policy of Congress to encourage the use by vessels of ports for handling cargo that would naturally move through such ports.

The Port of Stockton has the right to compete with other ports on the basis of the natural conditions confronting each port, without artificial devices in the form of rebates to draw traffic away from it to a competing port.

The Court should reverse the Commission's conclusion that port equalization against the Port of Stockton on cargo loaded at San Francisco or any other port located on San Francisco Bay is lawful.

The Court should hold that the findings hereinabove specified are unsupported by substantial evidence, and that when correct principles of law are applied in conjunction with the unchallenged findings of fact and conclusions in the majority Report, port equalization on such cargo results in (1) a violation of the policy of Section 8 of the Merchant Marine Act, 1920, (2) a violation of Section 15

of the Shipping Act, 1916, in that such port equalization is contrary to the public interest, (3) a violation of Section 205 of the Merchant Marine Act, 1936, (4) unlawful rebates in violation of Section 16 (Second) of the Shipping Act, 1916, and (5) unfairness and unjust discrimination and undue prejudice against the Port of Stockton in violation of Sections 15 and 16 (First) of the Shipping Act, 1916.

The Commission's Order should be declared invalid, permanently enjoined and set aside to the extent that it orders the respondents before the Commission to omit from their rules the characterization of cargo as that "which would normally move" from certain ports, and to the extent that it fails to order the respondents before the Commission (a) to cease and desist from applying their equalization rules to cargo equalized against the Port of Stockton and loaded at San Francisco or any other port located on San Francisco Bay, and (b) to modify their equalization rules to exclude their application to cargo loaded at such ports.

This case should be remanded to the Commission with instructions to revise its Order in accordance with the immediately preceding paragraph. (See *Mitchell v. United States*, 313 U.S. 80, 85 L. Ed. 1201, 61 Sup. Ct. 873; *Henderson v. United States*, 339 U.S. 816, 94 L. Ed. 1302, 70 Sup. Ct. 843.)

Respectfully submitted,

ALBERT E. CRONIN, JR.
(Albert E. Cronin, Jr.)
320 Wells Fargo Bank Building
Stockton, California 95202

J. RICHARD TOWNSEND
(J. Richard Townsend)
Route 2, Box 294,
Martinez, California 94553

*Attorneys for Petitioner
Stockton Port District*

Dated: June 22, 1966

Certificate of Counsel and of Service

I certify that, in connection with the preparation of this brief, I have examined Rules 18 and 19 of the United States Court of Appeals for the Ninth Circuit, and that, in my opinion, the foregoing brief is in full compliance with those rules.

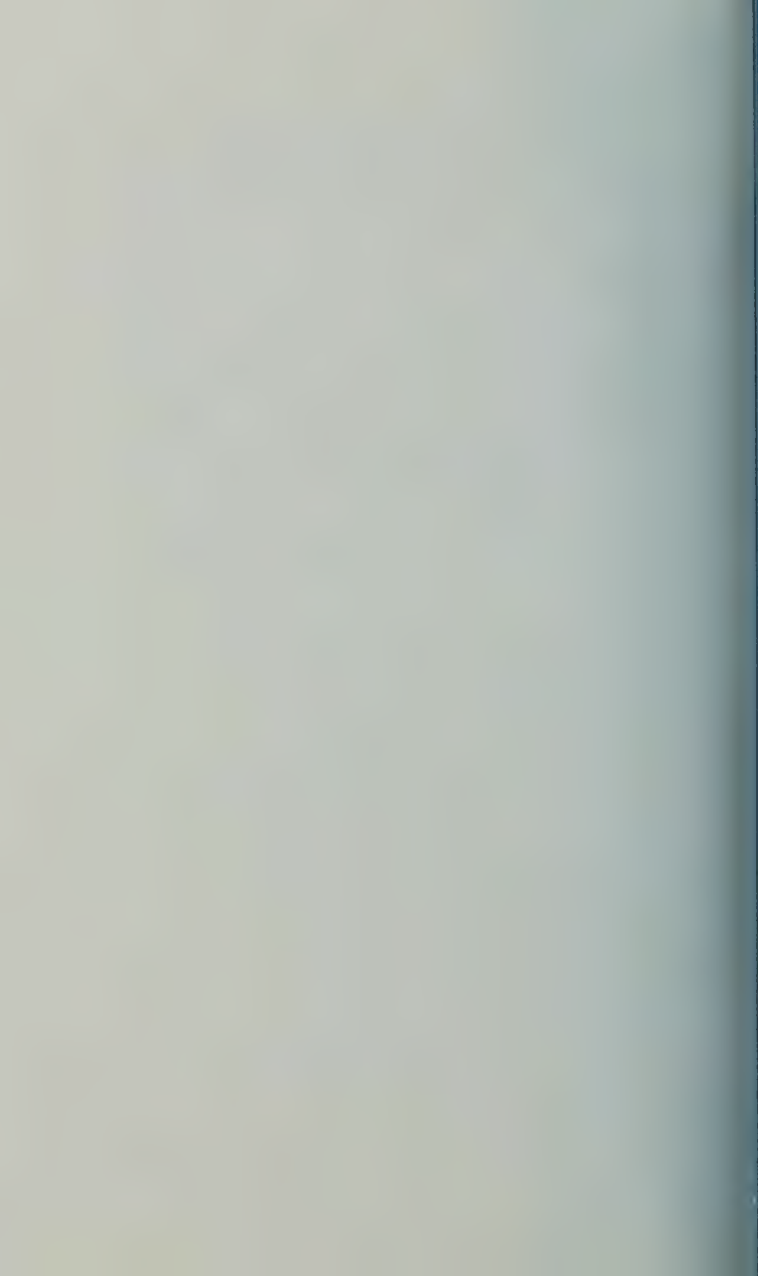
I further certify that I have this day served the foregoing document upon all parties of record in this proceeding by mailing, by air mail, postage prepaid, three copies to Walter Mayo III, attorney for the respondents, and one copy to Irwin A. Seibel, Attorney, Department of Justice, and by mailing a copy thereof, by regular first-class mail, postage prepaid, to Edward D. Ransom, attorney for interveners Pacific Westbound Conference and its members, Leonard G. James, attorney for interveners Pacific Straits Conference and Pacific/Indonesian Conference and their members, and Miss Miriam E. Wolff, attorney for intervenor San Francisco Port Authority.

Dated at San Francisco, California, June 22, 1966.

J. RICHARD TOWNSEND
(J. Richard Townsend)

*Attorney for Petitioner
Stockton Port District*

(Appendices A, B and C Follow)



the 1990s, the number of people in the world who are undernourished has increased from 600 million to 800 million.

There are a number of reasons for this. First, the world population has increased by 1.5 billion in the last 20 years. Second, the world population is ageing, and the elderly are more likely to be undernourished. Third, the world population is becoming more urban, and urban populations are more likely to be undernourished.

There are a number of reasons for this. First, the world population is becoming more urban, and urban populations are more likely to be undernourished. Second, the world population is becoming more urban, and urban populations are more likely to be undernourished.

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APPENDIX A

Rule No. 2 of Pacific Westbound Conference

*(As set forth in Appendix A of Report of Federal
Maritime Commission in Docket No. 1086)*

(The "Equalization rule", so far as it relates particularly to the Port of Stockton, is underlined.)

Subject to Rules 5, 7 & 9, rates are based on direct loading at Conference terminal loading ports or docks. However, individual member lines may, in lieu of a direct call, absorb the cost of transshipment between terminal ports; or between terminal ports and non-terminal ports; also between non-terminal ports. Reference to non-terminal port absorption applies only if the non-terminal ports have the required minimum tonnage as specified in Rule No. 9, or elsewhere in this tariff. Carriers may equalize between terminal ports only from point of origin, as provided and subject to the limitations set forth herein.¹ Equalization is the absorption by the carrier of the difference between shipper's cost of delivery to ship's tackle at Terminal Dock at nearest conference terminal port and the cost of delivery to ship's tackle at terminal dock and port of equalizing line. Conference terminal ports and docks are those named in Rule No. 5. Conditions and limitations as to equalization follow:

1. In the Pacific Straits Conference rule and the Pacific/Indonesian Conference rule, the following appears in lieu of the foregoing four sentences:

Rates are based on direct loading at loading port or docks, but the individual member line Carriers may meet the competition of other member lines loading direct at terminal ports or docks, either by transshipment or by equalization from point of origin.

Otherwise the rules of the three conferences are substantially the same, insofar as they relate to the Port of Stockton.

(a) Equalization shall not exceed an absorption in excess of 35 percent of the ocean freight, including handling charges and wharfage.

(b) A carrier may not equalize between terminal ports and non-terminal ports, or between non-terminal ports or between docks within a port.

(c) When the inland cost of transportation from point of origin is lower to terminal ports in Oregon, Washington, or British Columbia than via California terminal ports, equalization may be applied via California terminal ports only on shipments of deciduous fruits and dairy products (See Note below covering Explosives) and such equalization shall be permitted only so long as there is not adequate service from the terminal port in Oregon, Washington, or British Columbia, to which the cargo is tributary, to meet the needs of shippers of these commodities.

NOTE: Equalization on explosives is not permitted except that in the event a shipper is unable to obtain space for a specific shipment of explosives by a direct sailing from a terminal through which explosives would normally move at a date which reasonably will meet the needs of such shipper or his consignee, equalization shall be permitted on such shipment, Provided, that the shipper certifies to the Conference the need for space on such date and allows 48 hours after receipt of such certification for the Conference to indicate the conference carriers who can provide space on a direct sailing which reasonably will meet the shipper's needs.

(d) Equalization is permitted on shipments of fresh fruits, which would normally be shipped via California terminal ports when shipped via terminal ports in Oregon, Washington, or British Columbia, when there is not adequate service from the California port, to which the cargo

is tributary, to meet the needs of shippers of these commodities.

(e) Cargo which would normally move from one terminal port in Oregon, Washington, or British Columbia, may be shipped under equalization through another terminal port in Oregon, Washington, or British Columbia, and cargo which would normally move from one California terminal port, may be shipped under equalization via another California terminal port.

(f) Equalization shall only be paid on the basis of the lowest applicable common carrier or contract carrier rates.

(g) In support of each claim for equalization the shipper must furnish the carrier a copy of transportation bill covering movement from point of origin.

(h) Prior to payment of equalization bills, Carriers must submit to the Conference on prescribed form a certified statement for confirmation and approval of applicable interior rates and/or the basis for equalization.

APPENDIX B**Statutes Relied Upon**

1.

Section 15 of Shipping Act, 1916 (46 U.S. Code 814)

"That every common carrier by water, or other person subject to this Act, shall file immediately with the Commission a true copy, or, if oral, a true and complete memorandum, of every agreement with another such carrier or other person subject to this Act, or modification or cancellation thereof, to which it may be a party or conform in whole or in part, fixing or regulating transportation rates or fares; giving or receiving special rates, accommodations, or other special privileges or advantages; controlling, regulating, preventing, or destroying competition; pooling or apportioning earnings, losses, or traffic; allotting ports or restricting or otherwise regulating the number and character of sailings between ports; limiting or regulating in any way the volume or character of freight or passenger traffic to be carried; or in any manner providing for an exclusive, preferential, or cooperative working arrangement. The term 'agreement' in this section includes understandings, conferences, and other arrangements.

The Commission shall by order, after notice and hearing, disapprove, cancel or modify any agreement, or any modification or cancellation thereof, whether or not previously approved by it, that it finds to be unjustly discriminatory or unfair as between carriers, shippers, exporters, importers, or ports, or between exporters from the United States and their foreign competitors, or to operate to the detriment of the commerce of the United States, or to be contrary to the public interest, or to be in violation of this Act, and shall approve all other agreements, modifications, or cancellations. * * *

2.

Section 16 (First) and (Second) of Shipping Act, 1916 (46 U.S. Code 815)

“* * * * *

That it shall be unlawful for any common carrier by water, or other person subject to this Act, either alone or in conjunction with any other person, directly or indirectly:

First. To make or give any undue or unreasonable preference or advantage to any particular person, locality, or description of traffic in any respect whatsoever, or to subject any particular person, locality, or description of traffic to any undue or unreasonable prejudice or disadvantage in any respect whatsoever: * * *.

Second. To allow any person to obtain transportation for property at less than the regular rates or charges then established and enforced on the line of such carrier by means of false billing, false classification, false weighing, false report of weight, or by any other unjust or unfair device or means.

* * * * *

3.

Section 8 of Merchant Marine Act, 1920 (46 U.S. Code 867)

“That it shall be the duty of the board, in cooperation with the Secretary of War, with the object of promoting, encouraging, and developing ports and transportation facilities in connection with water commerce over which it has jurisdiction, to investigate territorial regions and zones tributary to such ports, taking into consideration the economies of transportation by rail, water, and highway and the natural direction of the flow of commerce; to investigate the causes of the congestion of commerce at ports and the remedies applicable thereto; to investigate the subject

of water terminals, including the necessary docks, warehouses, apparatus, equipment, and appliances in connection therewith, with a view to devising and suggesting the types most appropriate for different locations and for the most expeditious and economical transfer or interchange of passengers or property between carriers by water and carriers by rail; to advise with communities regarding the appropriate location and plan of construction of wharves, piers, and water terminals; to investigate the practicability and advantages of harbor, river, and port improvements in connection with foreign and coastwise trade; and to investigate any other matter that may tend to promote and encourage the use by vessels of ports adequate to care for the freight which would naturally pass through such ports: *Provided*, That if after such investigation the board shall be of the opinion that rates, charges, rules, or regulations of common carriers by rail subject to the jurisdiction of the Interstate Commerce Commission are detrimental to the declared object of this section, or that new rates, charges, rules, or regulations, new or additional port terminal facilities, or affirmative action on the part of such common carriers by rail is necessary to promote the objects of this section, the board may submit its findings to the Interstate Commerce Commission for such action as such commission may consider proper under existing law."

4.

Section 205 of Merchant Marine Act, 1936 (46 U.S. Code 1115)

"Without limiting the power and authority otherwise vested in the Commission, it shall be unlawful for any common carrier by water, either directly or indirectly, through the medium of an agreement, conference, association, understanding, or otherwise, to prevent or attempt to prevent

any other such carrier from serving any port designed for the accommodation of ocean-going vessels located on any improvement project authorized by the Congress or through it by any other agency of the Federal Government, lying within the continental limits of the United States, at the same rates which it charges at the nearest port already regularly served by it."

5.

Section 7(d) of Administrative Procedure Act (5 U.S. Code 1006)

"RECORD.—The transcript of testimony and exhibits, together with all papers and requests filed in the proceeding, shall constitute the exclusive record for decision in accordance with section 8 and, upon payment of lawfully prescribed costs, shall be made available to the parties. Where any agency decision rests on official notice of a material fact not appearing in the evidence in the record, any party shall on timely request be afforded an opportunity to show the contrary."

6.

Section 10(e) of Administrative Procedure Act (5 U.S. Code 1009)

"SCOPE OF REVIEW.—So far as necessary to decision and where presented the reviewing court shall decide all relevant questions of law, interpret constitutional and statutory provisions, and determine the meaning or applicability of the terms of any agency action. It shall (A) compel agency action unlawfully withheld or unreasonably delayed; and (B) hold unlawful and set aside agency action, findings, and conclusions found to be (1) arbitrary, capricious, an abuse of discretion, or otherwise not in accordance with law; (2) contrary to constitutional right, power, privilege or immunity; (3) in excess of statutory jurisdiction,

authority, or limitations, or short of statutory right; (4) without observance of procedure required by law; (5) unsupported by substantial evidence in any case subject to the requirements of sections 7 and 8 or otherwise reviewed on the record of an agency hearing provided by statute; or (6) unwarranted by the facts to the extent that the facts are subject to trial de novo by the reviewing court. In making the foregoing determinations the court shall review the whole record or such portions thereof as may be cited by any party, and due account shall be taken of the rule of prejudicial error."

7.

Fifth Amendment to Constitution of the United States

"No person shall * * * be deprived of life, liberty, or property, without due process of law; nor shall private property be taken for public use, without just compensation."

8.

Sections 2, 3 and 4 of Review Act of 1950 (5 U.S. Code 1032-1034)

"SEC. 2. The court of appeals shall have exclusive jurisdiction to enjoin, set aside, suspend (in whole or in part), or to determine the validity of * * * (c) such final orders of the United States Maritime Commission or the Federal Maritime Board or the Maritime Administration entered under authority of the Shipping Act, 1916, as amended, and the Intercoastal Shipping Act, 1933, as amended, as are now subject to judicial review pursuant to the provisions of section 31, Shipping Act, 1916, as amended, * * *

Such jurisdiction shall be invoked by the filing of a petition as provided in section 4 hereof.

"SEC. 3. The venue of any proceeding under this Act shall be in the judicial circuit wherein is the residence of

the party or any of the parties filing the petition for review, or wherein such party or any of the such parties has its principal office, or in the United States Court of Appeals for the District of Columbia.

“SEC. 4. Any party aggrieved by a final order reviewable under this Act may, within sixty days after entry of such order, file in the court of appeals, wherein the venue as prescribed by section 3 hereof lies, a petition to review such order. * * *”

APPENDIX C**Record Reference to Exhibits Offered Before Commission
in Docket No. 1086**

(Numbers hereinafter set forth indicate pages of Reporter's Transcript before the Commission, which are the same as the pages of the Court Record)

Exhibit No.	Identified	Offered	Received or Rejected*
1	9	10	11
2	13	13	14
3	14	15	15
4	17	58	58
5	23	23	24
6	23	23	24
7	29	29	29
8	36	42	55
9	55	56	56
10	59	61	62
11	68	68	68
12	69	69	70
13	71	72	72
14	72	73	73
15	74	76	76
16	77	80	80
17	83	85	85
18	86	88, 92	88, 92
19	93	95	95
20	96	98	99
21	105	106	106
22	107	108	108
23	109	109	109
24	110	116	116
25	126	126	126
26	170	172	173
27	170	172	173
28	176	177	178
29	242	254	256

*All exhibits offered were received in evidence, except those where the page number shown in this column is in parenthesis, and such exhibits were rejected.

Exhibit No.	Identified	Offered	Received or Rejected*
30	265	291	297
31	267	291	297
32	271	291	297
33	273	291	297
34	274	291	297
35	278	291	297
36	301	301	(334)
37	346	348	353
38	354, 355	Not Offered	
39	354, 355	362	364
40	365	370	375
41	375	376	380
42	509	522	524
(Withdrawn)			
43	633	633	634
44	653	661	663
45	653	663	663
46	654	664, 671	671
47	654	673	676
48	655	677	683
49	655		735
50	655	685	686
51	656	687, 701	703
52	656	688	691
53	656	700	701
54	657	706	708
55	657	709	711
56	767	771	771
57	774	776	778
58	837	838	839
59	1,106	1,107	1,108
60	1,112	1,113	1,113
61	1,118	1,119	1,119
62	1,118	1,119	1,119
63	1,140	1,142	1,142
64	1,168	1,171	1,172
65	1,175	1,176	1,177
66	1,183	1,185	1,185
67	1,186	1,188	1,188

BRIEF FOR RESPONDENTS

FEB 14 1967
FEDERAL MARITIME COMMISSION AND UNITED STATES OF AMERICA

IN THE UNITED STATES COURT OF APPEALS
FOR THE NINTH CIRCUIT

No. 20,544

STOCKTON PORT DISTRICT,

Petitioner,

v.

FEDERAL MARITIME COMMISSION and UNITED STATES OF AMERICA,

Respondents.

ON PETITION FOR REVIEW OF ORDER OF
THE FEDERAL MARITIME COMMISSION

DONALD F. TURNER
Assistant Attorney General

IRWIN A. SEIBEL
Attorney

Department of Justice

August 12, 1966

JAMES L. PIMPER
General Counsel

ROBERT N. KATZ
Solicitor

WALTER H. MAYO, III
Attorney
Federal Maritime Commission
Washington, D. C. 20573

FILED

AUG 12 1966

WM. B. LUCK, CLERK

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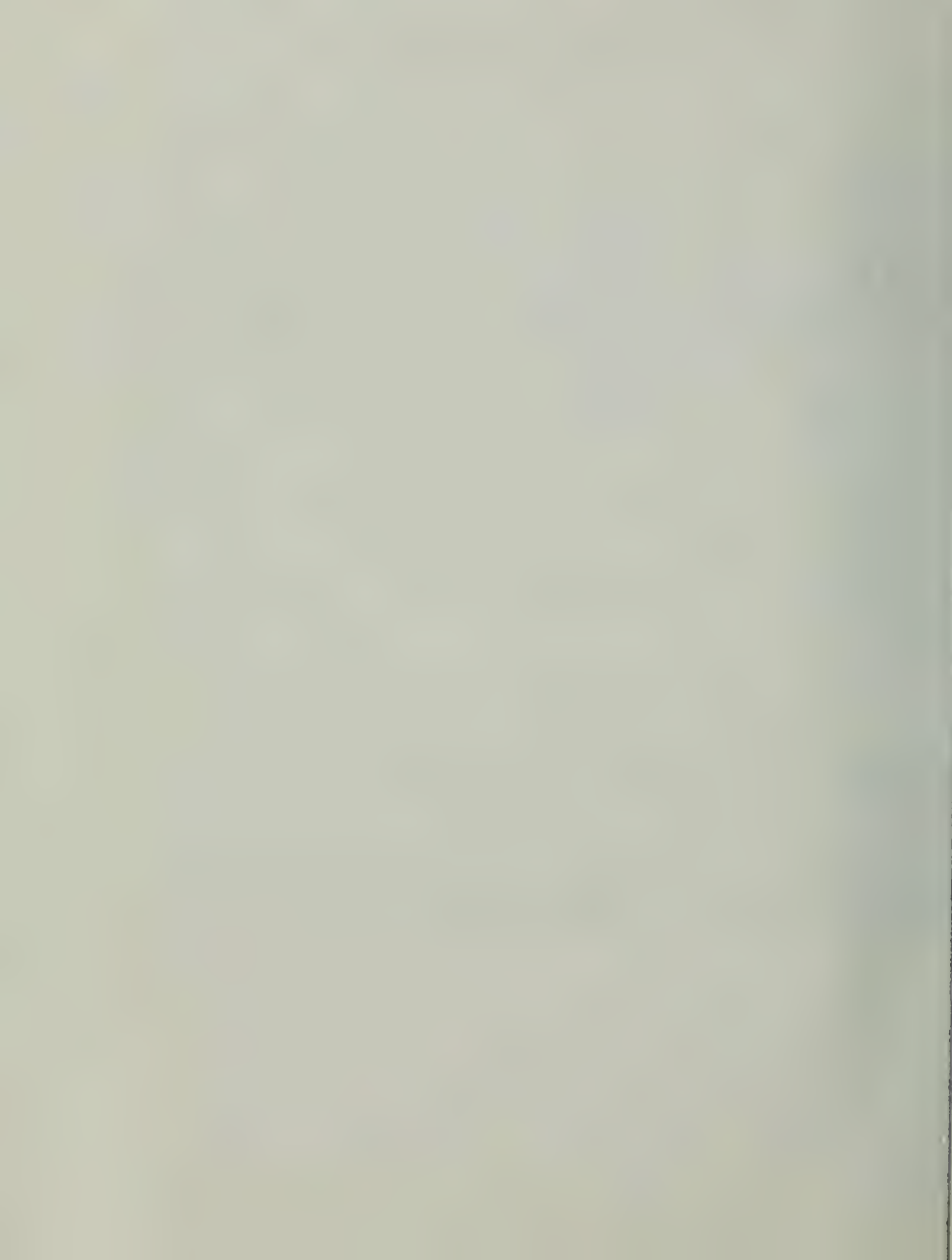


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COUNTERSTATEMENT OF THE CASE

This is a petition to review a Report and Order of the Federal Maritime Commission dated September 24, 1965, as amended September 28, 1965, issued in the Commission's Docket No. 1086, Stockton Port District v. Pacific Westbound Conference, et al. The substance of the proceeding related to conference agreements and tariffs which permit port equalization whereby conference carriers may equalize inland transportation costs between terminal ports. Stockton Port District, the petitioner, urged the Commission to order the Conferences to delete the port equalization rules from conference tariffs.

The Hearing Examiner issued an initial decision on September 24, 1964. Exceptions were taken thereto and oral argument was held before the Commission. The Hearing Examiner concluded and the Commission found that equalization as practiced by the Conferences against Stockton was lawful under the Shipping Act, 1916, but that equalization on cargo loaded at Long Beach and Los Angeles was unjustly discriminatory and unfair to terminal ports in the San Francisco Bay area. The petitioner contended that the agreements of the Conferences and the conference tariffs, are prejudicial to the Port of Stockton and contrary to statutory provisions.

The tariff rules which Stockton seeks to have declared unlawful provide that a carrier may reimburse a shipper for the difference between the shipper's inland transportation costs to Stockton, if it is nearer, and the shippers' inland transportation costs to any San Francisco Bay area terminal port of loading. Thus, the total outbound cost is the same to the shipper regardless of which of the two ports is used. Stockton alleges that this results in diversion of cargo normally tributary to Stockton. The volume of outbound



argo moving from Stockton has increased considerably in recent years. Since August 1957 the Port of Stockton has had phenomenal growth. (C.R. 5, R. 1270)^{1/}

On the basis of evidence considered, the Commission treated Stockton as an integral part of the San Francisco Bay "harbor complex" and thus as being within the same "geographical area" which has access to the open sea through the Golden Gate. The territory surrounding Stockton and the entire bay area was found by the Commission to be centrally, economically and naturally served by the Conference vessels at San Francisco. The Commission also found that the areas naturally tributary to Stockton were equally naturally tributary to San Francisco.

ARGUMENT

Petitioner urges existence of numerous errors which may be reduced to the following issues:

1. Was the conclusion of the Federal Maritime Commission that the ports of San Francisco and Stockton are both "bay area" ports and in the same geographical area" supported by substantial evidence?
2. Was the conclusion that the equalization practices complained of here were not unjustly discriminatory and unlawful, as reached by the Federal Maritime Commission, arbitrary, capricious, an abuse of discretion and not supported by substantial evidence?
3. Was the decision of the Federal Maritime Commission contrary to applicable law?

^{1/} C.R. refers to the Commission Report of September 24, 1965.



THE CONCLUSION OF THE FEDERAL MARITIME COMMISSION THAT THE PORTS OF SAN FRANCISCO AND STOCKTON ARE BOTH "BAY AREA" PORTS AND IN THE SAME "GEOGRAPHICAL AREA" IS SUPPORTED BY SUBSTANTIAL EVIDENCE, AND IS NOT ARBITRARY, CAPRICIOUS, AN ABUSE OF DISCRETION OR ERRONEOUS.

The Commission considered testimony of witnesses, examined economic data historical background of the area as well as government publications in determining that Stockton and San Francisco were both bay area ports in the harbor complex and in the same geographical area. The Commission, in opinion, quoted from Acts of the California Legislature, Harbors and Navigation Code § 1908 which defined the San Francisco Bay Area as

"that region served by commercial shipping and transportation passing through the Golden Gate, including tributary areas of central and Northern California." (C.R. 12, R. 1277)

Commission did not rely upon petitioner's assertion of physical separation being sufficient to establish Stockton as being in a separate area from San Francisco. The Commission stated that mileage alone is not a determinative factor. It examined, as relevant, the economics of transportation and the natural flow of commerce. The Commission found that the natural direction of the flow of traffic from the San Joaquin valley is through the Golden Gate to the Pacific Ocean. The Commission further noted that San Francisco had been the principal port for such traffic for almost one hundred years before Stockton became a port. (C.R. 13, R. 1278)

This finding that the tributary territory of Stockton was wholly within the territory attributed to San Francisco was reinforced by a similar understanding as to the ports encompassed within the area as set forth in a joint



ication of the Maritime Administration, Department of Commerce and Corps
Engineers, Department of the Army, "The Ports of San Francisco and Redwood
, California" Port Series, No. 30, Rev. 1951. (C.R. 15, R. 1280)

The mere fact that the ports of Stockton and San Francisco are in the
port complex and geographic areas was not, however, the sole consideration
the Commission in finding lawful the equalization practices for cargo via
San Francisco.

THE CONCLUSION OF THE FEDERAL MARITIME COMMISSION THAT THE EQUALIZATION
OF CARGO VIA SAN FRANCISCO DID NOT RESULT IN UNJUST OR UNFAIR DISCRIMINATION
IS SUPPORTED BY SUBSTANTIAL EVIDENCE AND IS NOT ARBITRARY, CAPRICIOUS, AN
ABUSE OF DISCRETION, OR ERRONEOUS.

In making its determination that the equalization practices which it found
were not unfair or unjustly discriminatory the Commission considered
monopoly of shippers and carriers as well as port authorities. While Stockton
seemed to have lost \$232,000 in potential revenue as a result of equalization
practices, the Commission found the exact extent of the loss speculative.

(C.R. 13-14, R. 1278 and 1279) The Commission determined that notwithstanding
loss of some revenue there was "ample economic and cost justification for
discrimination against Stockton, such as it is." It found that it cost an
average additional amount of \$3,600 to send a vessel to Stockton and, therefore,
would have cost the carriers approximately \$67,000 more than the \$113,030
of equalization. (C.R. 14, R. 1279) It is an eight hour trip in each
direction for a vessel to go the additional distance to Stockton. The Commission
found that equalization procedures gave the carrier operational flexibility and
latitude in loading and scheduling. It further found that equalization is
substantially cheaper than transshipment (C.R. 7, R. 1272) and that the fewer



ing ports in an itinerary, the better will be the operating results of the
rier. While the Commission recognized that elimination of equalization would
beneficial to the Port of Stockton and perhaps some of the shippers in that
a, the Commission determined that equalization reflected an overall economic
ed, tangible benefit to the public at large, and an important transportation
stification. (C.R. 20, R. 1285) The Commission noted that even with equal-
ation Stockton experienced phenomenal growth since 1957. (C.R. 22, R. 1287)
therefore, concluded that the prejudice or discrimination against Stockton
sulting from equalization in favor of San Francisco was not so undue or unjust
to warrant disapproval.^{2/}

In urging this Court to set aside the findings of the Commission the
itioner has merely made charges and allegations. Petitioner argues that
e findings and conclusions of the Federal Maritime Commission are arbitrary,
pericious and not supported in fact. The petitioner has not, however, sustained
e burden required of it in urging this position. Section 10(e) of the
Administrative Procedure Act (5 U.S.C. 1006) gives a reviewing court authority
"set aside agency action, findings and conclusions found to be (1) arbitrary,
pericious [or] an abuse of discrimination... [or] (5) unsupported by substantial

The foregoing is dispositive of petitioner's contentions that the decision
approves an agreement in violation of sections 15 and 16 (First), Shipping
Act, 1916.



evidence" The Supreme Court has defined substantial evidence

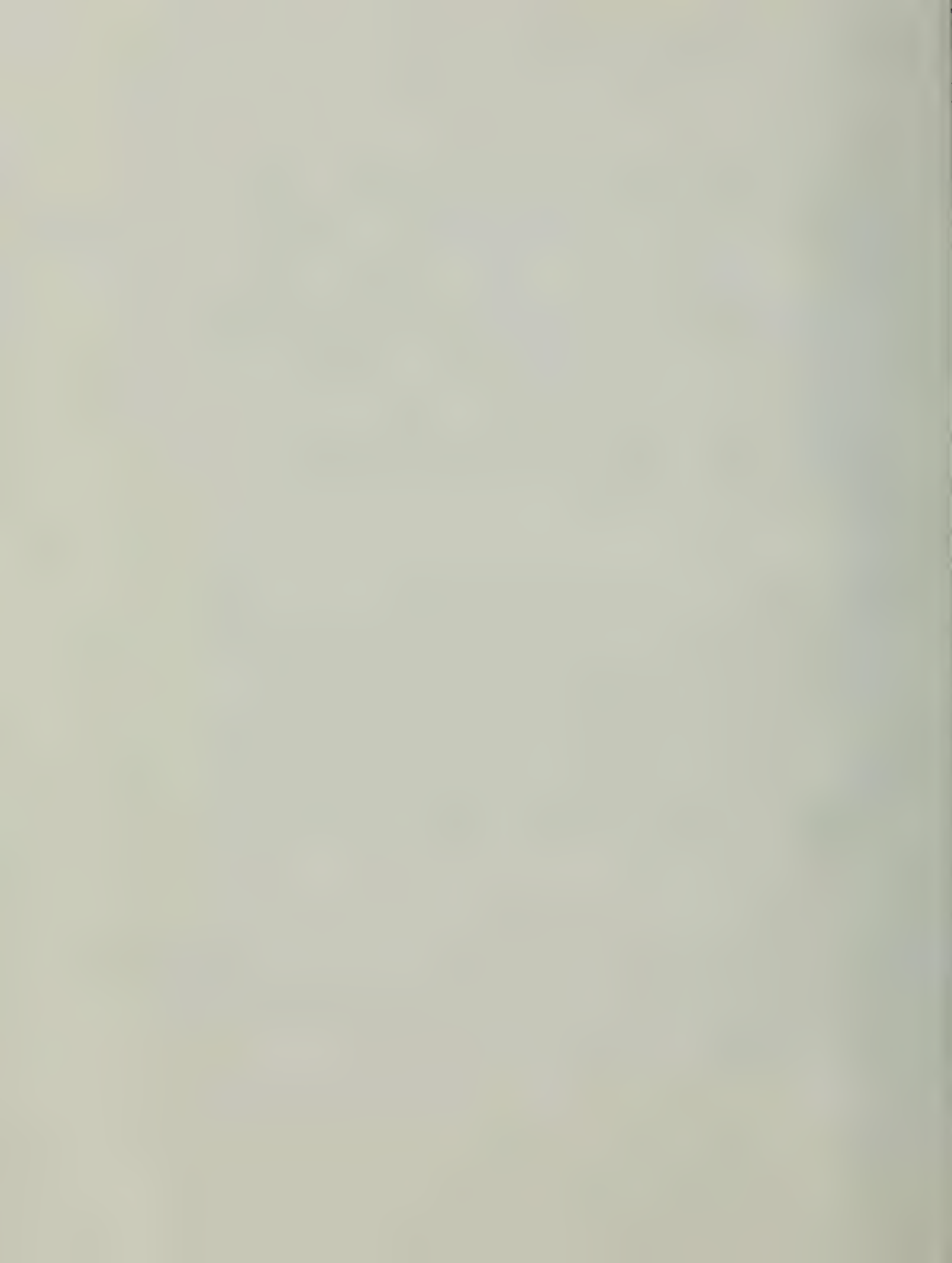
as:

"such relevant evidence as a reasonable mind might accept as adequate to support a conclusion." Consolidated Edison Co. v. Labor Board, 305 U.S. 197, 229. "[I]t must be enough to justify, if the trial were to a jury, a refusal to direct a verdict when the conclusion sought to be drawn from it is one of fact for the jury." Labor Board v. Columbian Enameling & Stamping Co., 306 U. S. 292, 300. This is something less than the weight of the evidence, and the possibility of drawing two inconsistent conclusions from the evidence does not prevent an administrative agency's finding from being supported by substantial evidence. Labor Board v. Nevada Consolidated Copper Corp., 316 U. S. 105, 106; Keele Hair & Scalp Specialists, Inc. v. FTC, 275 F. 2d 18, 21.

* * * * *

These policies are particularly important when a court is asked to review an agency's fashioning of discretionary relief. In this area agency determinations frequently rest upon a complex and hard-to-review mix of considerations. By giving the agency discretionary power to fashion remedies, Congress places a premium upon agency expertise, and, for the sake of uniformity, it is usually better to minimize the opportunity for reviewing courts to substitute their discretion for that of the agency. Consolo v. Federal Maritime Commission, et al., 383 U. S. 607 at 620, 621 (1966). (Footnotes omitted).

The major issue to which the Commission had to address itself was whether or not there was undue or unreasonable prejudice or discrimination. The conclusions of the Commission on this issue should not be set aside since there is evidence to support them.



"Whether a discrimination in rates or services of a carrier is undue or unreasonable has always been regarded as peculiarly a question committed to the judgment of the administrative body, based upon an appreciation of all the facts and circumstances affecting the traffic."

Swayne & Hoyt, Ltd. et al. v. U. S., 300 U.S. 297 at 304 (1937). See also, U. S. Navigation Co. v. Cunard Steamship Co., 284 U.S. 474 (1931)

itioner also urges that because the Commission found unjust discrimination equalization as practiced against Stockton in connection with citrus fruits in Southern California the Commission must also find unjust discrimination equalization against Stockton in favor of San Francisco and it must now be that equalization between San Francisco and Stockton be disallowed. However, this alleged inconsistency merely serves to demonstrate that the Commission considered the evidence of different facts and different circumstances arriving at a different conclusion for two separate circumstances and conditions. With reference to equalization in favor of Southern California the Commission found that there would be diversion of traffic from areas not normally naturally tributary to Southern California and that there would be undue prejudice and unjust discrimination.

To require an agency or court to arrive at the same conclusions based on different evidentiary findings is a new and novel legal theory. The Supreme Court dealt with this argument as follows:

"to hold otherwise would be to create the doubtful and perhaps dangerous precedent that the decision of the



Board in respect of one agreement definitely establishes that the rule of that decision must, without more, be applied to other agreements alleged to be of a similar character, although it may turn out upon investigation that the allegations are not warranted, or the facts and circumstances surrounding the transaction are so wholly different as to afford grounds for a different result." U. S. Navigation Company v. Cunard Steamship Co., 284 U.S. 474 at 488, (1931).

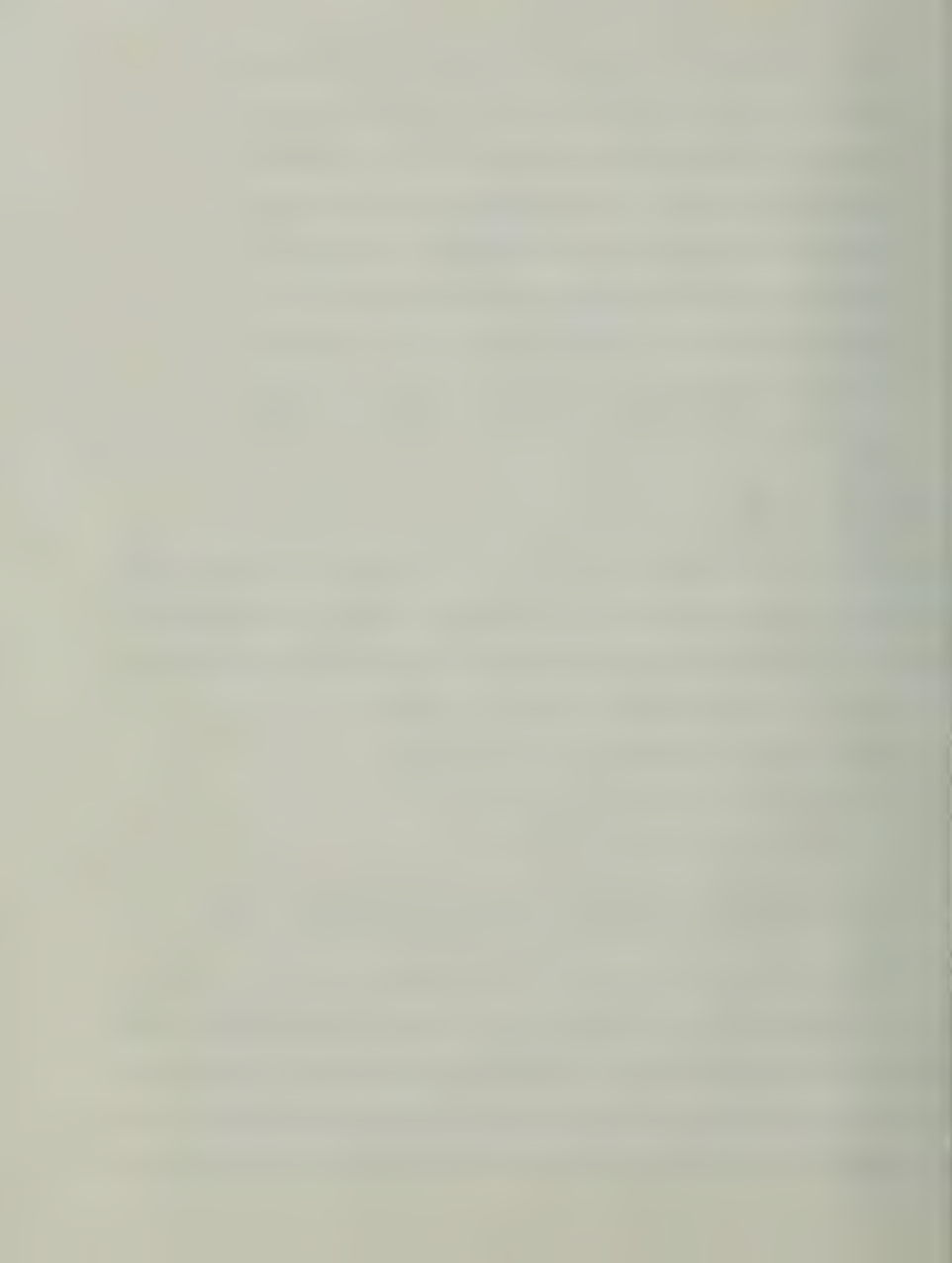
PORT EQUALIZATION IS NOT UNLAWFUL

The concept of port equalization is not illegal per se and petitioner does not urge illegality per se. Petitioner does, however, allege that the decision of the Commission approves a practice which violates the following:

- a. Section 8 of the Merchant Marine Act of 1920.
- b. Section 205 of the Merchant Marine Act, 1936.
- c. Section 16 of the Shipping Act, 1916.
- d. Section 15 of the Shipping Act, 1916.

A. THE DECISION OF THE COMMISSION DOES NOT UPHOLD VIOLATION OF SECTION 8 OF THE MERCHANT MARINE ACT, 1920

Petitioner alleges that section 8 of the Merchant Marine Act, 1920 should be held applicable to condemn the port equalization practices herein involved on the ground that section 8 expresses the intent of the Congress to favor port improvement and development and to encourage the use by vessels of ports adequate to care for the freight which would naturally pass through



m. 3/ Petitioner relies upon the case of Pacific Far East Line v. United States,
F. 2d 711 (C.A., D.C. 1957). That decision, however, merely approved the act

Section 8 provides:

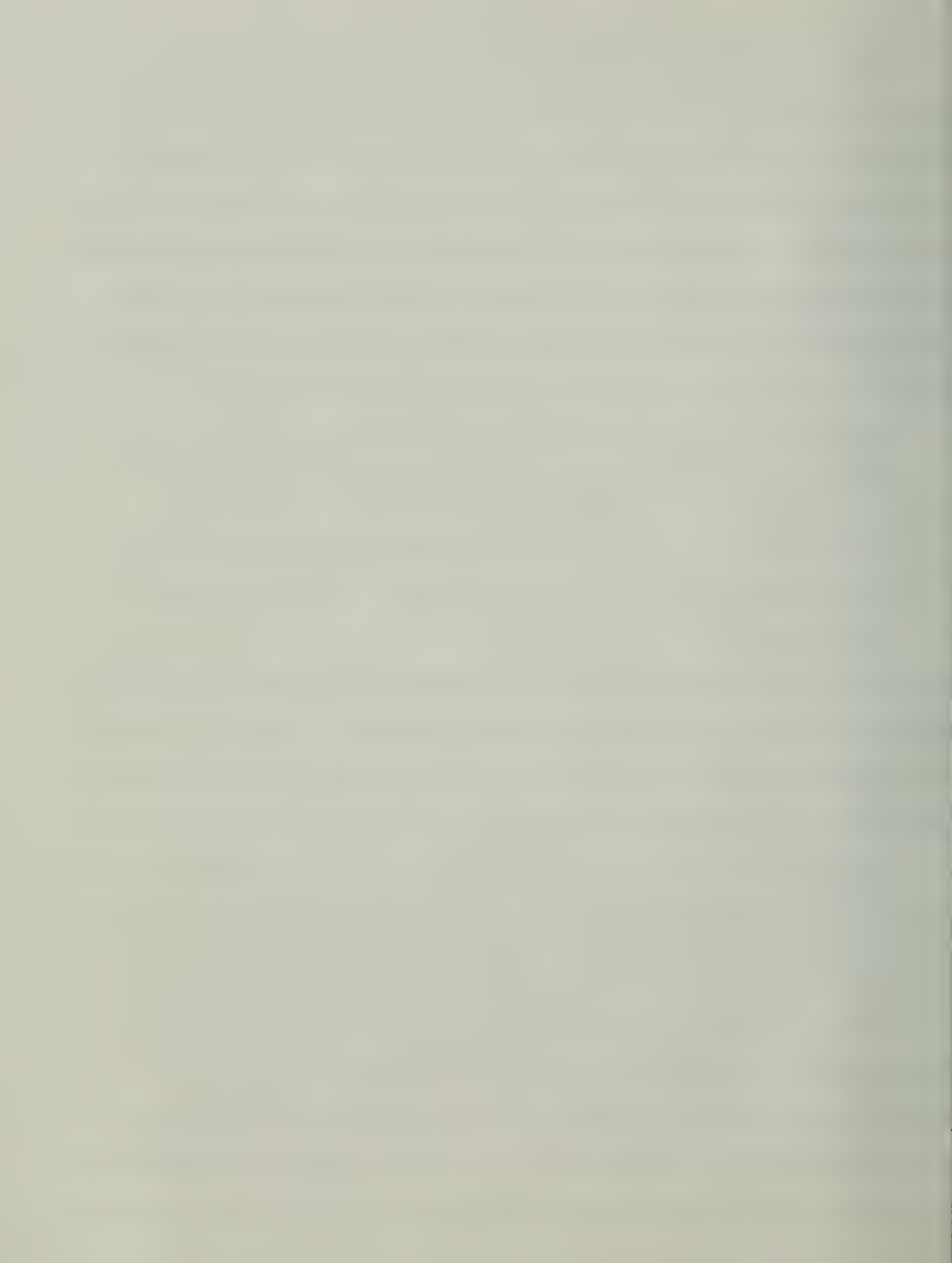
"That it shall be the duty of the board, in cooperation with the Secretary of War, with the object of promoting, encouraging, and developing ports and transportation facilities in connection with water commerce over which it has jurisdiction, to investigate territorial regions and zones tributary to such ports, taking into consideration the economies of transportation by rail, water, and highway and the natural direction of the flow of commerce; to investigate the causes of the congestion of commerce at ports and the remedies applicable thereto; to investigate the subject of water terminals, including the necessary docks, warehouses, apparatus, equipment, and appliances in connection therewith, with a view to devising and suggesting the types most appropriate for different locations and for the most expeditious and economical transfer or interchange of passengers or property between carriers by water and carriers by rail; to advise with communities regarding the appropriate location and plan of construction of wharves, piers, and water terminals; to investigate the practicability and advantages of harbor, river, and port improvements in connection with foreign and coastwise trade; and to investigate any other matter that may tend to promote and encourage the use by vessels of ports adequate to care for the freight which would naturally pass through such ports: Provided, That if after such investigation the board shall be of the opinion that rates, charges, rules, or regulations of common carriers by rail subject to the jurisdiction of the Interstate Commerce Commission are detrimental to the declared object of this section, or that new rates, charges, rules, or regulations, new or additional port terminal facilities, or affirmative action on the part of such common carriers by rail is necessary to promote the objects of this section, the board may submit its findings to the Interstate Commerce Commission for such action as such commission may consider proper under existing law."

the Federal Maritime Board, predecessor of the Federal Maritime Commission, examining certain practices in the light of the policy set forth in section 8. The Board found the practice therein involved to be unfair and unjustly discriminatory on the basis of the facts. The Board relied upon the policy set forth in section 8 in arriving at its decision. The Court upheld the decision of the Board and the authority of the Board to consider section 8 in making its determinations. The Board was merely free to examine the issue raised in the light of the policy of section 8. The court stated as follows:

"That policy having been expressed, the Board could, if it was not bound to do so, examine the practices here complained of in the light of that policy, and exercise its power to approve or disapprove such practices accordingly." (Emphasis supplied.)
246 F.2d at 716.

arriving at the conclusions which petitioner seeks to have set aside the Commission did consider policies set forth in section 8. (CR 12, R. 1277)

It is clear that the Commission considered regions and zones tributary to the ports involved, economics of transportation, the natural direction of the flow of commerce, and facilities of the ports, as well as the policy set forth in section 8. Having examined the issues and evidence in the light of section 8, the Commission exercised its power to approve the equalization practices. In so doing the Commission recognized the economics of equalization as compared with transshipment (C.R. 21, R. 1286) and it considered the welfare of the carriers, shippers and general public. It had determined that while some traffic was diverted from Stockton there was, in the region and zone involved, no diversion of traffic that was solely and exclusively tributary to Stockton



R. 13, R. 1288). Delineation of a "geographic area" will almost always
necessity involve the inclusion of parties whose inland ports will vary in
distance or in mileage. The Commission, exercising its expertise, delineated
the area involved and found the cargo traffic involved was naturally tributary
to both ports. (C.R. 16, R. 1291)

It further should be pointed out that section 8, in actuality, relates
primarily to rates, charges, rules or regulations of common carriers by rail,
and, therefore, except as a broad statement of policy, has no relationship to
rates, charges, rules or regulations of common carriers by water.

B. THE DECISION OF THE COMMISSION IS NOT CONTRARY TO
SECTION 205 OF THE MERCHANT MARINE ACT, 1936

Petitioner alleges that equalization as practiced against Stockton in
the case of San Francisco is in violation of section 205 of the Merchant Marine
Act, 1936.^{4/} It says that the equalization rule prevents a carrier, which
would otherwise send its vessel to Stockton, from serving Stockton. Petitioner
is mistaken.

Section 205 of the Merchant Marine Act, 1936 provides as follows:

"Without limiting the power and authority otherwise vested in
the Commission, it shall be unlawful for any common carrier
by water, either directly or indirectly, through the medium
of an agreement, conference, association, understanding, or
otherwise, to prevent or attempt to prevent any other such
carrier from serving any port designed for the accommodation
of ocean-going vessels located on any improvement project
authorized by the Congress or through it by any other agency
of the Federal Government, lying within the continental limits
of the United States, at the same rates which it charges at
the nearest port already regularly served by it."

No functions, with respect to this section of the 1936 Act were transferred
to the Federal Maritime Commission by Reorganization Plan No. 7 of 1961 which
established the Commission. Accordingly, the Commission in arriving at a
decision is not bound by the provisions of that section of the Act. At best
such provisions would be a guide for the Commission to follow in its deter-
mination. In any event as we point out in the text the Commission decision

Stockton is served at the same rates as the Conference charges at nearest ports regularly served by them, since rates are the same for all bay terminal ports. Other carriers are not precluded from or prevented from serving Stockton because of the necessity of being in competition with other carriers. The allegation of the petitioner is simply not founded in fact. The ultimate cost to shippers is the same regardless of whether shipment is through Stockton or another port such as San Francisco. There is sufficient evidence supporting this conclusion (C.R. of R. 1071) including evidence that carriers who are practicing equalization or have the rules of equalization available to them are serving the port of Stockton at various times. In 1962 the Pacific West Coast Conference members made a total of 133 calls at Stockton. Pacific Far East Line made 30 at Stockton, and American President Lines made 24 calls. Accordingly, there is nothing in the decision of the Commission or under the equalization rules involved herein that are not in conformity with section 205 of the Merchant Marine Act, 1936.

ON THE DECISION OF THE COMMISSION IS NOT
CONFORMANT TO SECTION 16 (SECOND) OF THE SHIPPING
ACT, 1916

Petitioner alleges that the practices involved result in an unlawful rate in violation of section 16 (second) of the Shipping Act, 1916 (46 U.S.C. 816). This contention is without foundation. Discrimination against a shipper is necessarily measured by what the shipper pays, not by what the carrier ultimately collects. Under similar circumstances the Commission, in Beaumont v. Seatrains Lines, 1 U.S. M.C. 693, found no evidence of discrimination against shippers. All shippers similarly situated pay the same

1 price for ocean carriage. The rules and practices of equalization are
ly and publicly set forth, tariffs are publicly filed and all shippers
ascertain what the total cost of shipments will be for themselves and other
pers similarly situated. Discrimination is measured by what the shippers
and shippers who receive equalization pay the same amount for through
sportation whether they ship via Stockton or San Francisco.

The practices outlawed by section 16 of the Shipping Act of 1916 are
e practices which would allow a person to obtain transportation at
than regular rates by means of false billings, false reports, false
sifications or other unfair, unjust devices and means. These are not
lved in the equalization rules or practices. The entire transaction is
losed. The limitations and restrictions of section 16 of the Shipping
are directed to surreptitious activities. See Ambler, et al. v. Blodel
van Lumber Mills, (CA 9 1933) 68 F.2d. 268, at 271 and Hohenberg Brothers
v. Federal Maritime Commission, 316 F.2d 381 at 385 (CADC 1963).

D. THE DECISION OF THE FEDERAL MARITIME COMMISSION IS
NOT CONTRARY TO SECTION 15 AND 16 OF THE SHIPPING ACT, 1916

Petitioner alleges that the equalization rules and practices are violative
ections 15 and 16 (First) of the Shipping Act, 1916 in that they are unfair,
stly discriminatory and unduly prejudicial against the Port of Stockton.
Commission properly found as discussed earlier, under point II, that there
no unfairness, undue prejudice or unjust discrimination.

In view of the foregoing it would appear that petitioner's contention
rest upon an allegation that equalization is illegal per se. However,

an argument was not set forth because such an argument would be clearly
discriminatory. Only when there is unfair or unjust discrimination would such a
practice be illegal. There have been no decisions in which equalization between
ports on the same harbor or ports having common tributary areas has been dis-
approved. See Beaumont Port Commission v. Seatrain, 2 USMC 699. The concept
of rate adjustment to meet competition by carriers has been upheld in numerous
decisions. To deny rate equalization if pressed to its logical conclusion
generally "would result in traffic flowing only through the most distant
red port." Boston & Marine Railroad v. United States, 202 F. Supp.
837 (USDC Mass., 1962).

CONCLUSION

The Federal Maritime Commission fully and adequately supported its findings
based on extensive evidence considered by it and by the Hearing Examiner. The
Commission distinguished the equalization practices herein involved from those
which were disapproved in other proceedings. The Commission found that the
equalization practices with reference to San Francisco were not unfair, un-
justly discriminatory or unduly prejudicial to the Port of Stockton, a type
of finding which courts have found to be primarily and peculiarly within the
province of the administrative agency. The Commission followed the applicable
law in arriving at its decision. The Commission further indicated in its
decision that it considered all issues raised by the petitioner whether or not
it addressed itself specifically to them. In much the same manner that peti-
tioner bombarded the Commission with numerous ill-conceived exceptions to the
Hearing Examiner's decision, the petitioner has bombarded this Court with alleged

ors in its attempt to grasp upon some basis for justifying the setting aside
the Commission's findings and decision. The petition should be dismissed.

Respectfully submitted,

WALD F. TURNER
Assistant Attorney General

JAMES L. PIMPER
General Counsel

WIN A. SEIBEL
Attorney
U. S. Department of Justice

ROBERT N. KATZ
Solicitor

August 12, 1966
Washington, D. C.

WALTER H. MAYO III
Attorney

Federal Maritime Commission

CERTIFICATE OF COUNSEL AND OF SERVICE

I certify that, in connection with the preparation of this brief, I examined Rules 18 and 19 of the United States Court of Appeals for Ninth Circuit, and that, in my opinion, the foregoing brief is in full compliance with those rules.

I further certify that I have this day served three copies of the foregoing brief via first-class airmail, postage prepaid, upon the following:

Art E. Cronin, Jr., Esq.
Wells Fargo Bank Building
Oakton, California 95202

J. Richard Townsend, Esq.
Route 2, Box 294
Martinez, California 94553

Harold G. James, Esq.
Sam James & Rolph
Sansome Street
San Francisco, California

Miriam E. Wolff, Esq.
State of California
Department of Justice
State Building
San Francisco, California 94102

Harold D. Ransom, Esq.
Wick, Geary, Wheat, Adams & Charles
California Street
San Francisco, California 94104

Dated at Washington, D. C. this 11th day of August 1966.

Walter H. Mayo III
Attorney
Federal Maritime Commission

FEB 14 1967

No. 20544

In the
United States Court of Appeals
For the Ninth Circuit

STOCKTON PORT DISTRICT,

Petitioner,

vs.

FEDERAL MARITIME COMMISSION AND
UNITED STATES OF AMERICA,

Respondents.

Reply Brief of Petitioner
Stockton Port District

ALBERT E. CRONIN, JR.
320 Wells Fargo Bank Building
Stockton, California 95202

J. RICHARD TOWNSEND
Route 2, Box 294,
Martinez, California 94553

*Attorneys for Petitioner
Stockton Port District*

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Dated: September 12, 1966



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vs.

FEDERAL MARITIME COMMISSION AND
UNITED STATES OF AMERICA,

Respondents.

Reply Brief of Petitioner Stockton Port District

I.

INTRODUCTION

The Brief of Intervenor Pacific Westbound Conference and Its Member Lines states :

“The Commission and the Examiner both concluded * * * that areas naturally tributary to Stockton are equally so to, and can be naturally served at, San Francisco and the other ports within the same geographical area. * * *” (PWC Brief 6.)*

*Throughout this Brief all emphasis in quotations is supplied unless otherwise stated.

This points up very clearly the fallacy in the decision of the Federal Maritime Commission under consideration and in the position of the respondents and their supporting intervenors.

If the San Joaquin Valley area, which is naturally tributary to the Port of Stockton, can, as our opponents contend, be also served "naturally" at San Francisco, then there is no need for the artificial device of port equalization in order to influence the movement of the cargo via San Francisco instead of Stockton. Of course the truth of the matter—and the basis of our complaint—is that the area that is naturally tributary to Stockton because of lower inland transportation rates cannot be served "naturally" at San Francisco, but requires the artificial device of port equalization in order to be served at San Francisco.

Our complaint is directed to the unfair and artificial means of port equalization which is employed by the intervenor ocean carriers in order to influence the movement of this cargo via San Francisco and thus deprive the Port of Stockton of freight which would naturally pass through Stockton except for such equalization.

The briefs of the respondents and their supporting intervenors do not meet the issues that we have raised, but attempt to divert attention away from the real issues by expounding on such irrelevant matters as whether Stockton is a San Francisco Bay Harbor Complex port (whatever that is), whether Stockton is in the same "geographical area" as San Francisco, whether the area that is "naturally tributary" to Stockton is also "naturally tributary" to San Francisco, and the so-called "transportation economics" involved in moving the cargo in question via San Francisco instead of Stockton.

We shall refer to the various issues mentioned in our Opening Brief and will show that the briefs of the respond-

ents and their intervenors do not meet the arguments that we have advanced under the respective issues.

II.

SECTION 8 OF MERCHANT MARINE ACT, 1920

In and by Section 8 of the Merchant Marine Act, 1920, (46 U.S.C. 867), Congress has declared that "the use by vessels of ports adequate to care for the freight which would naturally pass through such ports" shall be promoted and encouraged.* Congress has thus determined that such action is in the public interest.

The Federal Maritime Board recognized its duty in this respect in the case of *City of Portland v. Pacific Westbound Conference*, 4 F.M.B. 664 (1955), in the following language:

"Section 8 charges the Board with the duty to promote and encourage the use by vessels of ports adequate to care for the freight which would naturally pass through such ports." (4 F.M.B. 679.)

In the *City of Portland* case the Board likewise held that Section 8 requires as follows:

"* * * That section requires, all other factors being substantially equal, that a given geographical area and its ports should receive the benefits of or be subject to the burdens naturally incident to its proximity to another geographical area.* * *" (4 F.M.B. 679.)

In upholding the Board's decision in the *City of Portland* case, the United States Court of Appeals held with respect to Section 8 in *Pacific Far East Line v. United States*, 246 F. (2d) 711 (C.A., D.C., 1957):

"* * * That policy having been expressed, the Board could, if it was not bound to do so, examine the practices complained of in the light of that policy, and

*The statutes relied upon by petitioner are set forth in Appendix B of its Opening Brief.

exercise its power to approve or disapprove such practices accordingly. * * *” (246 F. (2d) 716.)

Section 8 of the Merchant Marine Act, 1920, is the law of the land, and the policy of Congress expressed therein must be followed by the Federal Maritime Commission, as well as having been followed by the Federal Maritime Board.*

As we pointed out in our Opening Brief (pages 5, 15-16), 47,529 tons of cargo were equalized by the respondent Conference lines against the Port of Stockton in 1962, and of that amount 46,129 tons moved over ports located on San Francisco Bay. (Ex. 11-14.) The Commission has found that “Without equalization much of the cargo would move through Stockton”. (Com. Rep. 7-8, R. 1272-73.) The reason for this is that the inland transportation rates are lower to the Port of Stockton from the area involved—namely the San Joaquin Valley—than to any other port. (Rep. Tr. 731, Rollins; Ex. 4, 10, 30, 32, 33, 34.)

Except for the artificial device of port equalization, therefore, in the language of Section 8 the freight in question “would naturally pass through” the Port of Stockton.

The Commission therefore is required to comply with its duty to enforce the Congressional policy expressed in Section 8—namely to prohibit the port equalization which prevents freight that would naturally pass through the Port of Stockton from doing so.

But our opponents set forth various arguments in an unconvincing effort to show that Section 8 does not compel such a result.

*A comparison of Reorganization Plan No. 51 of 1950 and Reorganization Plan No. 7 of 1961 shows that the powers granted to the Federal Maritime Board and the Federal Maritime Commission were the same. (See 46 U.S.C.A. 1111 note.)

They contend that the Commission considered Section 8, but concluded that there were other factors that outweighed the policy expressed by Congress in Section 8—such as “transportation economics”, including the interests of shippers, carriers desiring to equalize, and other ports. But Congress has expressed the policy which it desires to have followed, and it did not leave room for the Commission to determine whether it disagreed with Congress. As the Board said in the *City of Portland* case, (supra, page 3), Section 8 created a duty and a requirement for the Commission to follow. In the case of *Pacific Far East Line v. United States*, supra, in upholding the decision of the Board in the *City of Portland* case the United States Court of Appeals intimated that the Board should examine equalization practices in the light of the Congressional policy expressed in Section 8 and should exercise its power to approve or disapprove such practices “accordingly”—that is, on the basis of whether the equalization practices produced results contrary to the policy expressed by Congress in Section 8. Since the equalization practices here involved divert from the Port of Stockton cargo which would otherwise naturally pass through that port, such practices are clearly in violation of the Congressional policy expressed in Section 8, and the Commission should therefore have performed its duty to require the discontinuance of such equalization practices.

Our opponents likewise argue that the policy expressed in Section 8 is inapplicable here because the Port of Stockton and the ports on San Francisco Bay are in the same “geographical area” and the area that is naturally tributary to the Port of Stockton is also naturally tributary to San Francisco and other ports located on San Francisco

Bay. There is nothing in Section 8 making the policy expressed therein inapplicable when ports in the same geographical area are involved. With respect to "naturally tributary" territory, the question under Section 8 is through which port the freight in question would "naturally pass"—that is, in the absence of artificial devices such as port equalization. Here the Commission has found that such freight would pass through the Port of Stockton. The Congressional policy expressed in Section 8 is therefore clearly applicable to the present situation.

By its policy expressed in Section 8, Congress has determined that it is in the public interest to promote and encourage the use by vessels of ports for freight which would naturally pass through such ports. Since the Commission has found that without equalization much of the equalized cargo would move through the Port of Stockton (Com. Rep. 7-8, R. 1272-73), and since the port equalization rules and practices divert such cargo away from Stockton, Section 8 requires the Commission to comply with the Congressional policy by ordering the discontinuance of such equalization rules and practices.

The Commission should have exercised its power under the Shipping Act, 1916, by ordering the discontinuance of the port equalization rules and practices here involved on the ground that they violate the Congressional policy expressed in Section 8 of the Merchant Marine Act, 1920, and hence are unjustly discriminatory between ports and contrary to the public interest, in violation of Section 15 of the Shipping Act, and unduly preferential and prejudicial between ports, in violation of Section 16(First) of the Shipping Act.

III.

SECTION 205 OF MERCHANT MARINE ACT, 1936

In their replies to our argument pertaining to Section 205 of the Merchant Marine Act, 1936, (46 U.S.C. 1115), (our Opening Brief, 22-23), the respondents and their supporting intervenors simply refuse to recognize that the Commission has made the following finding of fact in its Report:

“* * * Although equalization is optional under the tariff, carriers find that competition compels them to equalize.” (Com. Rep. 8, R. 1273.)

Since competition compels carriers to equalize, this obviously produces the result that a Conference carrier whose managerial judgment would lead it to serve the Port of Stockton by sending its vessel to Stockton to load cargo, is compelled by the competitive equalization practices of other Conference carriers to refrain from sending its vessel to Stockton and instead to equalize the cargo via another port, such as San Francisco.

The equalization rule, and the practice of the Conference members thereunder, have thus prevented the carrier in question from serving Stockton. This is a clear violation of Section 205.

IV.

UNLAWFUL REBATES

The respondents and their intervenors argue that here there cannot be any unlawful rebates under Section 16 (Second) of the Shipping Act, 1916, (46 U.S.C. 815), because, they claim, under that section the reduced rates must result in a situation where there is some sort of concealment or misrepresentation and here everything was set forth in the tariff.

The Commission found that if there were no equalization some of the cargo in question would still have moved via San Francisco without any payment by the ocean carrier of any part of the shipper's inland transportation charges. (Com. Rep. 8, 14 R. 1273, 1279.) (See our Opening Brief, 24.) The payment of part of the shipper's inland transportation charges is, as we stated in our Opening Brief (page 24), a purely unnecessary gratuitous rebate—an unjust and unfair device which enables the shipper to obtain transportation at less than the regular rates or charges. Compare *Investigation of Storage Practices of Pacific Far East Line, Inc., et al.*, 6 F.M.B. 301 (1961), which is cited on page 25 of our Opening Brief.

Even if some form of concealment or misrepresentation were required under Section 16(Second), it is readily present in this situation. The tariff of the respondent Conferences which was involved in the hearing before the Commission allowed equalization only under the following circumstances:

“* * * cargo which would normally move from one California terminal port, may be shipped under equalization via another California terminal port.” (See paragraph (e) of Appendix A of our Opening Brief.)

When equalization payments were made on cargo which would have moved over San Francisco without any equalization, there has been a payment by the ocean carrier of part of the shipper's inland transportation charge in violation of the tariff, since the cargo in question would not normally have moved over Stockton. This is clearly the kind of concealment or misrepresentation which our opponents contend is required in order to constitute an unlawful rebate under Section 16(Second).

UNJUST DISCRIMINATION AGAINST PORT OF STOCKTON

We have shown that there is unjust discrimination and undue prejudice against the Port of Stockton because the equalization rules and practices violate the Congressional policy expressed in Section 8 of the Merchant Marine Act, 1920. But there is unjust discrimination and undue prejudice against Stockton on another ground, which will be discussed next.

As we pointed out in our Opening Brief, the Commission found that port equalization resulted in unjust discrimination against the Port of Stockton in the case of cargo equalized against Stockton which was loaded at Los Angeles or Long Beach. The Commission found that there was no unjust discrimination against Stockton, however, when the same cargo was equalized against Stockton and loaded at San Francisco or any other port located on San Francisco Bay. The reason for this difference in treatment was that the Commission found that the Port of Stockton was a San Francisco Bay area port and hence Stockton and San Francisco were in the same "geographical area", and that the area naturally tributary to Stockton was also "naturally" tributary to San Francisco.

The Brief of the Pacific Westbound Conference refers continually to "San Francisco Bay Harbor Complex Ports". The Commission did not make any finding with respect to any "harbor complex"—whatever that term means. The Examiner used the term "harbor complex", but the Examiner's Initial Decision is not part of the Commission's Report. In its Report the Commission approved some of the Examiner's conclusions, but it did not adopt his Initial Decision as its decision. Consequently, the Examiner's Initial Decision cannot be used to support findings

or conclusions in the Commission's Report, and the quotations from the Initial Decision which are set forth in the Brief of the Pacific Westbound Conference are out of order and improper.

The briefs of the respondents and their supporting intervenors endeavor to make great capital of the fact that the Commission found that Stockton and San Francisco are in the same geographical area and that the area naturally tributary to Stockton is also naturally tributary to San Francisco. They have not advanced any contentions in this respect which we have not met fully at pages 25 to 45 of our Opening Brief. We showed there in considerable detail that there is no substantial "evidence" to support these findings, and that even if such findings were correct, they would not be a proper ground for differentiating between the Los Angeles and San Francisco situations and for concluding that there is no unjust discrimination against the Port of Stockton when the cargo is loaded at San Francisco, even though there is unjust discrimination when it is loaded at Los Angeles or Long Beach.

The respondents and their intervenors also rely heavily on economic factors in an attempt to defeat our claim of unjust discrimination and undue prejudice against the Port of Stockton. But the Commission itself has rejected economic considerations as a ground for determining whether there is unjust discrimination. In this connection the Commission concluded:

"* * * Thus, there is ample economic and cost justification for the discrimination against Stockton such as it is. But even this would not save respondents' equalization under the applicable precedents were it established that the practice drew cargo away from territory which was exclusively and naturally tributary to Stockton." (Com. Rep. 14, R. 1279.)

In considering the question of unjust discrimination, however, the Commission became confused in dealing with various terms, such as "naturally tributary", "natural direction of the flow of traffic", and "right to the traffic".

In finding unjust discrimination against Stockton resulting from equalization against that port when the cargo was loaded at Los Angeles or Long Beach, the Commission concluded that since the inland transportation costs were lower to Stockton than to Los Angeles or Long Beach, the area in which the traffic originated (the San Joaquin Valley) was "naturally tributary" to Stockton, and that consequently Stockton had a right to the traffic. The Commission concluded further that since the equalization destroyed this right it was unduly prejudicial to Stockton. (Com. Rep. 26, R. 1291.) That is the sense in which the terms "naturally tributary" and "right to the traffic" have been used in prior decisions. (See the quotations cited on pages 35, 38 and 39 of our Opening Brief from *City of Portland v. Pacific Westbound Conference*, 4 F.M.B. 664, 674-675; *City of Mobile v. Baltimore Insular Line, Inc.*, 2 U.S.M.C. 474, 486; *Beaumont Port Commission v. Seatrail Lines, Inc.*, 3 F.M.B. 556, 566.) In other words, in the case of cargo loaded at Los Angeles or Long Beach the Commission held that each port should stand on its own natural footing, and that cargo cannot be diverted from a port by the artificial device of port equalization.

The Commission proceeded to reverse its own conclusion when comparing San Francisco and Stockton. Even though inland transportation costs are lower to Stockton than to San Francisco from the San Joaquin Valley (a necessary ingredient for equalization and also a clear definition of naturally tributary territory), the Commission stated that the reverse of the Los Angeles/Long Beach conclusion was the correct approach.

The inland transportation costs from the San Joaquin Valley are lower to Stockton than to either San Francisco or Los Angeles and hence that area is naturally tributary to Stockton in both instances. The Commission should have concluded that since equalization destroyed Stockton's right to this traffic and Stockton was unduly prejudiced thereby when equalized over Los Angeles, the same undue prejudice existed when cargo from this origin area was equalized over San Francisco.

When the question is unjust discrimination and undue prejudice against Stockton in the case of the same cargo equalized against Stockton and loaded at San Francisco, the Commission has improperly applied a different meaning to the terms "naturally tributary" and "right to the traffic". Through some strange use of the term "naturally tributary", the Commission has concluded that the area which is naturally tributary to Stockton is also "naturally" tributary to San Francisco and that hence Stockton has no right to the traffic in question.

We have shown the invalidity of the Commission's position at pages 25 to 45 of our Opening Brief. We merely desire to remind the Court again of something that is wholly obvious. There can never be port equalization in a situation where the cargo is "naturally" tributary to the port at which the cargo is loaded, because the whole function and meaning of port equalization is an artificial device to divert the traffic away from the port over which it would naturally move and to force its movement over another port over which it would not move but for the equalization. The cargo thus cannot possibly be said to be naturally tributary to the forced loading port.

With respect to the proper meaning of the term "natural direction of the flow of traffic", the dissenting opinion of Commissioner Hearn has correctly described the situation as follows:

"Secondly, to say, as does the majority, that the 'natural direction of the flow of traffic from the San Joaquin Valley . . . is through the Golden Gate to the Pacific Ocean' begs the question. The point at issue is whether the 'natural direction of the flow of traffic from the San Joaquin Valley . . . through the Golden Gate . . . ' is through San Francisco or through Stockton. I hold to the belief that this natural flow is through Stockton, and succinctly stated, but for the equalization, an admittedly artificial device, San Joaquin exports would normally flow through the Golden Gate via Stockton * * *." (Com. Rep. 31, R. 1297.)

Perhaps we should reply briefly to the Pacific Westbound Conference's objection to our "incredible assertion" that "the Commission has not made any finding that port equalization on cargo loaded at San Francisco is justified by inadequacy of service at Stockton". (See PWC Brief 23 and our Opening Brief 41.) The only mention of this matter in the Commission's Report is as follows, which confirms the statements at page 41 of our Opening Brief:

"Service is unquestionably adequate at San Francisco. However, adequacy of service at Stockton is dependent upon the needs of particular shippers. Some shippers consider the Stockton service inadequate to meet overseas commitments." (Com. Rep. 8, R. 1273.)

The dissenting opinion of Commissioner Hearn has correctly set forth the legal principles applicable in determining the issue of unjust discrimination and undue prejudice against the Port of Stockton, in the following language:

"The only valid test, in this case, for determining whether or not the effectuation of the equalization rule, and consequently for determining whether respondents are giving 'any undue or unreasonable preference or advantage to any particular person, locality, or des-

cription of traffic' or subjecting 'any particular person, locality, or description of traffic to any undue or unreasonable prejudice or disadvantage' in violation of Section 16(First), is whether the traffic would move via San Francisco but for the equalization. Here, certainly, most of it would not and to the extent that the artificial device draws traffic from Stockton it is unlawful." (Com. Rep. 32, R. 1298. Underscoring in text.)

The Commission's conclusion that the equalization rules and practices are not unjustly discriminatory or unduly prejudicial against the Port of Stockton on cargo loaded at San Francisco or any other port on San Francisco Bay should be set aside by the Court because such conclusion is based on findings unsupported by substantial evidence and a failure to apply the correct principles of law.

VI.

SCOPE OF JUDICIAL REVIEW

The Brief of the Pacific Westbound Conference contends that the points that we have raised are not within the scope of proper judicial review, and that we are merely asking the Court to substitute its views on the facts for those of the Commission.

That this point is wholly without merit is apparent from the fact that the Federal Maritime Commission, which is continually involved in petitions for judicial review of its orders, does not even raise the point in its Brief.

The contentions that we have advanced are directed toward errors of law—improper construction of statutes or failure to apply statutes properly, lack of substantial evidence to support Commission findings, and absence of proper findings to support conclusions. These are all proper matters for judicial review.

CONCLUSION

Other points raised in the opposing briefs are adequately covered in our Opening Brief.

Once again we desire to direct the Court's attention to Commissioner Hearn's dissenting opinion (Com. Rep. 27A-33, R. 1293-99) for a correct statement of the principles of law on the various points which the majority of the Commission decided erroneously.

Our position is not that the Port of Stockton has an inalienable right to any particular cargo, but that Stockton should have the right to compete for any cargo without the added burden of an artificial barrier imposed by ocean carriers which deprives Stockton of this right to compete on a natural basis.

The Port of Stockton is entitled to have all ports compete for cargo on the basis of their respective natural advantages and disadvantages, free from artificial devices, such as port equalization, which divert from Stockton to a competing port cargo which would otherwise move over Stockton. This is in accordance with the Congressional policy expressed in Section 8 of the Merchant Marine Act, 1920, and with proper legal principles pertaining to unjust discrimination and undue prejudice.

The Commission's order should be set aside to the extent, and on the grounds, sets forth in our Opening Brief.

Respectfully submitted,

ALBERT E. CRONIN, JR.
320 Wells Fargo Bank Building
Stockton, California 95202

J. RICHARD TOWNSEND
Route 2, Box 294
Martinez, California 94553

*Attorneys for Petitioner
Stockton Port District*

Dated: September 12, 1966

CERTIFICATE OF COUNSEL AND OF SERVICE

I certify that, in connection with the preparation of this brief, I have examined Rules 18 and 19 of the United States Court of Appeals for the Ninth Circuit, and that, in my opinion, the foregoing brief is in full compliance with those rules.

I further certify that I have this day served the foregoing document upon all parties of record in this proceeding by mailing, by air mail, postage prepaid, three copies to Walter H. Mayo III, attorney for the respondents, and one copy to Irwin A. Seibel, Attorney, Department of Justice, and by mailing a copy thereof, by regular first-class mail, postage prepaid, to Edward D. Ransom, attorney for interveners Pacific Westbound Conference and its members, Leonard G. James, attorney for interveners Pacific Straits Conference and Pacific/Indonesian Conference and their members, and Miss Miriam E. Wolff, attorney for intervenor San Francisco Port Authority.

Dated at San Francisco, California, September 12, 1966.

J. RICHARD TOWNSEND

*Attorney for Petitioner
Stockton Port District*

FEB 14 1967

No. 20544

In the
United States Court of Appeals
For the Ninth Circuit

STOCKTON PORT DISTRICT,
Petitioner,
vs.
FEDERAL MARITIME COMMISSION AND UNITED
STATES OF AMERICA,
Respondents.

REPLY BRIEF OF INTERVENER

STATE OF CALIFORNIA

THOMAS C. LYNCH, Attorney General
of the State of California;

MIRIAM E. WOLFF, Deputy Attorney
General of the State of California

6000 State Building
San Francisco, California 94102
Phone: 557-3820

Attorneys for Intervener,
State of California

FILED

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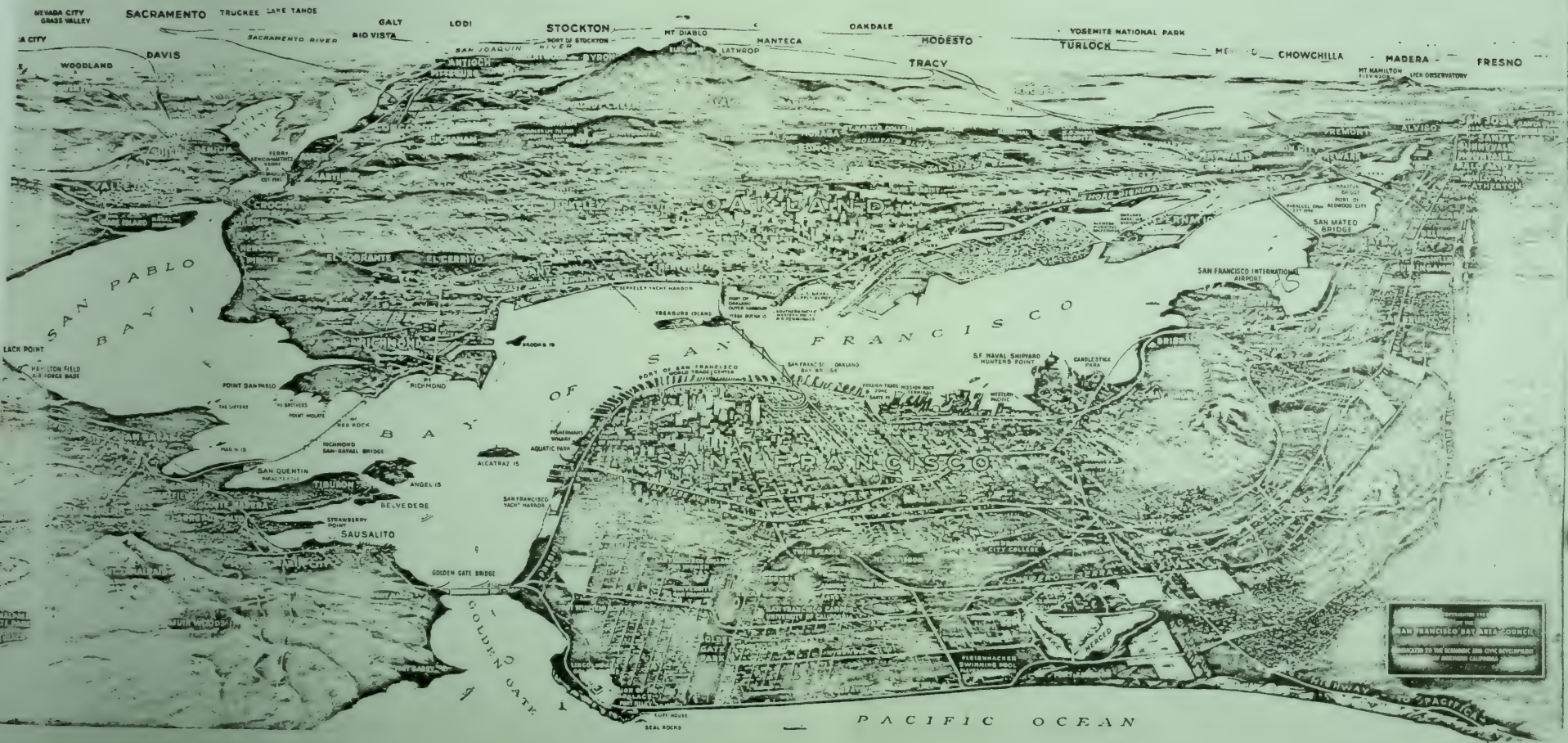
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San Francisco Bay Area Council
Established 1942
Coordinated to the economic and civic development
of the San Francisco Bay Area
San Francisco, California

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REPLY BRIEF OF INTERVENER

STATE OF CALIFORNIA

INTRODUCTION

The State of California intervened in this case on behalf of its agency the San Francisco Port Authority and in support of the position of respondents in the original docket. It has petitioned and has been granted leave to intervene in this court in support of the decision of the Federal Maritime Commission.

STATEMENT OF FACTS

Because the facts are outlined in detail in the decision of the Commission and have been discussed extensively in the brief of the Pacific Westbound Conference we shall endeavor to confine this discussion, in so far as possible, to a statement of the position of this intervener, the State of California.

The State of California has, for over 100 years, operated the Port of San Francisco through an agency now known as the San Francisco Port Authority and formerly called the Board of State Harbor Commissioners for San Francisco Harbor. The Port furnishes approximately seventy-six deep-water berths supplied with transit sheds, highway and rail facilities (1108, 1110-11)* for steamship lines connecting San Francisco and through it the State of California with approximately three hundred world ports (1118).

The Bay of San Francisco serves the entire geographic area. Immediately across the Bay from San Francisco are the deep-water facilities of Oakland, Encinal and Richmond. Southerly from San Francisco lies the deep-water Port of Redwood City, primarily a bulk port. The Army Base at Oakland also has deep-water facilities. Going up what is called San Pablo Bay we find specialized terminals located at Oleum, Rodeo, Hercules,

*Page references are to the Reporter's Transcript unless otherwise noted.

Pinole, Crockett and Selby. There are also oil ports at Avon and Martinez. Deep-water facilities of private companies are located at Pittsburg and Antioch. Up the Sacramento River we now have the new Port of Sacramento and up the San Joaquin River the Port of Stockton (Ex. 60). To show the profusion of deep-water berths in the Bay we attach to the facing page a reproduction of Exhibit 60, which shows locations although it does not show distances. Not all of the facilities mentioned have terminal status in the Pacific Westbound Conference but that Conference has afforded terminal status to Alameda, Oakland, Richmond, Stockton and Sacramento in addition to San Francisco (1117). Vessels may, of course, also have occasion to shift for specialized or military cargo.

The Port of San Francisco is entirely self-supporting. It was created without expense either to the State of California or the federal government and does not obtain funds from any tax roll. Major improvements are financed through general obligation or revenue bonds. Because maintenance of older structures has been so expensive, the Port is presently engaged in building new facilities financed through the issuance of \$26,000,000 in general obligation bonds (1143-1144). These bonds and earlier bonds issued and outstanding will have to be repaid through Port revenues. Any material decrease in those revenues would seriously affect the financial ability of the Port to service

its outstanding obligation (1144).

The tonnages of the Port of San Francisco have remained virtually static for the last few years although the tonnages of the Port of Stockton have risen dramatically (144). This relation in Stockton-San Francisco traffic is also reflected in the tonnage figures of the Pacific Westbound Conference itself (Exs. 44, 46). All of the ports in the Bay compete with one another for cargo. To accomplish this San Francisco, like the other ports, has maintained an active solicitation program (1130-1131). Largely by reason of this, the number of stops which a carrier is now expected to make in the Bay has created a monstrosly uneconomic situation with vessels commonly making three or four or more stops in this highly confined area (765-66, 793-95). The only economic means of protection which the carrier has is equalization and this it can and should utilize where the competing ports serve the same tributary territory. This is the basis of the Commission's decision.

Wharfage and dockage rates of the Port of San Francisco and the Port of Stockton are identical (Exs. 61, 62). Since terminal rates are the same and steamship rates are required by law to be the same, San Francisco endeavors to attract cargo on the basis of its superior number of direct sailings; its tempo-rate climate which is frequently of benefit to more perishable cargo and its wider range of facilities (1131). It is the

position of this intervener that all of San Francisco Bay and the ports which feed into it must for purposes of determining tributary territory, be considered as a single basin. In that basin certain ports have tended to become specialized. San Francisco, because of its location, is predominantly a general cargo port, a port with last loading for the Pacific Westbound, Pacific Straits and Pacific Indonesian Conferences and thus a port which establishes itself as particularly attractive for perishables. It is the position of this intervener that all of the terminal ports in this area should be treated as one group rather than considered as isolated ports with separate tributary territory (1132).

The Port of San Francisco is located on the point of a thin peninsula of land bounded on one side by the Pacific Ocean and on the other by the Bay of San Francisco (1120). If Stockton's position on tributary territory were to prevail, the Port of San Francisco which the State built and has maintained would have as its tributary territory a thin wedge of land lying along the Pacific Ocean roughly from San Luis Obispo to slightly below the Mendocino County line. Even this, however, would be subject on the Stockton theory, to the exceptions of territory tributary to Redwood City, Alameda, Oakland, Richmond and many other ports in the territory itself and even this would change at the whim of cities and counties which elected to bring deep-water facilities to their communities. The Stockton theory

of tributary territory is that where the inland mileage rate is cheaper to one terminal port than to another terminal port the territory from which it is cheaper is the tributary territory of the cheaper port (37, 43; Exs. 4, 8, 9).

The Federal Maritime Commission refused to accept this doctrine. In its decision the Commission stated:

"Stockton's argument for recognition of most of central California, including the great San Joaquin Valley, as its naturally tributary territory is based entirely upon minimum trucking rates to Stockton, which in turn are based upon the 'constructive mileage' between points of origin and Stockton. (Footnote omitted) Stockton contends that the examiner misconstrued the applicable precedents in finding that Stockton's tributary territory was also San Francisco's. As Stockton reads the cases 'tributary territory' is that area from which the inland transportation rates and mileages are less to a particular port than some other port. But Stockton's theory is only deceptively simple and does not comport with the principles laid down in prior cases. Under this 'constructive mileage' theory the naturally tributary territory expands and contracts with every new

highway innovation because constructive mileage changes with new bridges, traffic lights and the like. Under Stockton's theory the territory is dependent upon which ports are named 'terminal ports' by the carriers practicing the equalization. Thus, when the respondent Pacific Westbound Conference, but not the Straits or Indonesian Conferences, named Sacramento as a terminal port, Stockton's own witness, Mr. Phelps, stated that Stockton's tributary territory for the Pacific Westbound Conference was thereupon cut in half because 'that is the way the arithmetic comes out.'

"

"Although Stockton urges that the examiner's reliance on the Beaumont decision is misplaced we think it reasonable, well founded and proper. Moreover, the Maritime Administration, Department of Commerce, and the Corps of Engineers, Department of the Army, the governmental agencies charged with administering section 8, in their joint publication ('The Ports of San Francisco and Redwood City, Calif.' Port Series, No. 30, Rev. 1951.^{7/}) covering the port of San Francisco, described San Francisco as 'one of the most important ports for the vast inland territory of the Central and Pacific Coast

Area and the Intermountain States,' under the heading 'Tributary Territory.' In their publication covering Stockton, the 'Tributary territory' designated as that of Stockton is wholly within the territory attributed to San Francisco, and largely within the territory attributed to Oakland-Alameda in the publication covering those ports. It is obvious that these studies dictate a rejection of any 'constructive mileage' theory for determining 'naturally tributary territory.'

"We conclude, that for the purposes of this proceeding, the territory naturally tributary to Stockton should properly be considered naturally tributary to San Francisco and other San Francisco Bay area ports. . . ." (FMC Dec. pp. 14-16; R. 1279-1281.)

The Federal Maritime Commission based its decision on the principle that the equalization it permitted in this case reflected an overall economic good, was of tangible benefit to the public at large, and had an important transportation justification. (FMC Dec, p. 20; R. 1285.) The State agrees that the primary concern of the Commission, and thus of this court, must be the benefits to be regarded from the view of the overall public good. To the shipper equalization is a tremendous advantage. It enables cargo to reach

a vessel at the location best from the shipper's view. It enables the ship to have the operating latitude necessary if it is to serve a vast complex of terminal ports all located in one small area. It allows the seaports located farthest from the producing area but closest to the point at which the ocean voyage commences to compete with off ports located in the heart of the producing areas. In some instances it may even enable a shipper to compete in world markets he might otherwise lose (1133-1135; 1138).

Where a port in the hinterland has successfully solicited cargo, the ship if it is to accommodate the cargo, has only two alternatives if it cannot employ equalization. It can proceed to the port in question or it can transship by truck or barge at the carrier's expense. The Commission finds that the voyage to Stockton takes a vessel a minimum of eight hours in either direction. In addition, there are costs for pilotage, tugs and other incidental expenses, totaling approximately \$3,000 to \$4,000 per call. Transshipment costs the vessel approximately \$6.00 to \$7.50 per ton while equalization costs the vessel on the average of \$2.00 to \$2.50 per ton. (FMC Dec., p. 7; R. 1272.)

In the case of transshipment the owner has paid the cost of transportation to the nearest port and the port costs; the carrier must pay the cost of transportation to

the port of loading and in addition, it must pay all of the port costs at the loading port (761-763). It also involves rehandling of cargo which is undesirable both from the ship and the shipper's view (813-14; 845; 984; 1005; 1033; FMC Dec., p. 4; R. 1269).

Based on these primary considerations it is the State's position that the decision of the Commission is correct and should be affirmed.

If equalization were not permitted among all of the ports in the Bay area there is no question but that the Port of San Francisco would suffer serious financial damage. It is geographically further from the large producing area and since it exists on a thin peninsula of land served by busy highways and toll bridges inland transportation rates to San Francisco are commensurately greater. The Port of San Francisco was built and has been maintained in reliance on its revenues. Without an equalization rule those revenues can be seriously impaired (133; 1134-35; 1143-45). In constructing the port, the State relied on the fact the area it built served the entire region and would continue to do so. Had this not been so, San Francisco would have been forced to oppose other major improvement in the Bay and this would scarcely have served the public need. The Commission, in its decision, recognizes the basic principle and states:

"For almost a hundred years before Stockton was made accessible to oceangoing vessels, San Francisco was the principal port through which freight from the San Joaquin Valley would and did pass. It did not cease to be such a port merely upon the creation of an additional port at Stockton." (FMC Dec., p. 13; R. 1278.)

The economic health of the Port of San Francisco is of importance to the commerce of the United States both as a naval auxiliary and to meet certain requirements best served by ports located closest to the Golden Gate. In times of national emergency it is extremely important to have adequate existing facilities in good repair and geared to the efficient handling of cargo as close to the ocean as possible.

Considerations in support of the economic welfare of an important port are another basis for the position taken by the State in this case.

ARGUMENT

I

THE COMMISSION'S DECISION IS BASED ON SUBSTANTIAL EVIDENCE AND SHOULD BE AFFIRMED

The first question before any reviewing court is whether the decision of an administrative body is based on

substantial evidence. In this case the evidence is not only substantial but virtually uncontradicted. Both the carriers and shippers have testified that equalization, as permitted under the Conference provision, is of benefit to them and in the public interest (886-87; 909-979-80; 1032; 1086-87; 1138-39).

The Commission finds it would have cost approximately \$67,000 more to have sent fifty ships to Stockton than to have equalization (FMC Dec., p. 14; R. 1279). Obviously this additional cost is detrimental to the shipping public. The ability to equalize also carries affirmative benefits to the shippers. It insures frequent and regular service to meet shipping needs, the ability to meet delivery dates and assistance in the shipping of perishable products (811-12; 842-43; 905-6; 1031-1033). Only one shipper witness was presented by Stockton in support of its opposition to equalization and in his testimony it developed that his principal concern was not with equalization but with his endeavor to secure a greater amount of equalization than the Conference permitted (554-63; 574; 578-598). He then frankly admitted to the Examiner that he supported Stockton's position on the assumption that if there were no equalization there would be an adjustment in rates (601). Since the evidence conclusively proved that the cost of sending ships to Stockton would be more expensive than equalization the basis for his

opposition was conclusively dissipated.

While we are dealing with many ports and terminals in the Bay area we are concerned with only one harbor. With equalization the shipper and the steamship lines are at the mercy of numerous ports and terminals who have elected to compete with one another, frequently as a matter of local geographic pride. Equalization in this instance serves the interests of the steamship lines and the shipping public.

The steamship lines have devised two weapons for their own protection. One is transshipment. This is a costly and serious burden both to commerce and to the shipper whose goods are necessarily rehandled. If a part of the Federal Maritime Commission's function is to protect the commerce of the United States, we believe the Commission should, whenever possible, discourage transshipment in favor of equalization.

The second weapon is equalization. While the terminals tend to dislike the use of equalization when used against them, all fair-minded people would have to recognize from ship management's point of view and the shipper's viewpoint equalization is by far the soundest device. When ports are located in the hinterland of a single water complex, it stands to reason the shipper will tend to use the terminal closest to his point of origin to save every possible penny of inland

transportation costs. Even so, however, the trip to an additional berth for a single lot of cargo available at that moment may not be worth the cost of further shifting the vessel. We learned from the only steamship witness favorable to the Port of Stockton that even where his ships came to Stockton to load bulk or army cargo it was frequently not worth the cost of a shift to another berth in Stockton to pick up general cargo and that in instances his company had picked up that cargo by transshipment or equalization even though the vessel had actually called at Stockton (Ex.17).

Because of the numerous berths in the Bay area it is obvious a vessel could spend an unbelievable amount of time in this harbor shifting from competing port to competing port for odd lots of cargo. Such wasteful practices do not fulfill the needs of commerce.

The evidence on which the decision relies to support its conclusion that equalization is for the greater public good is uncontradicted. On review this court may not set aside the findings or conclusions of the Commission unless they are ". . . 'found to be (1) arbitrary, capricious, (or) an abuse of discretion . . . (or) (5) unsupported by substantial evidence. . . .'" The court has "defined 'substantial evidence' as 'such relevant evidence as a reasonable mind might accept as adequate to support a conclusion.' This is something less than the weight of the evidence, and

the possibility of drawing two inconsistent conclusions from the evidence does not prevent an administrative agency's finding from being supported by substantial evidence." Consolo v. FMC, ____ U.S. ____ (1966); 16 L.Ed. 2d 131.

II

THE COMMISSION'S DECISION IS IN ACCORDANCE WITH EXISTING LAW AND SHOULD BE AFFIRMED

There is nothing inherently unlawful about equalization. In determining whether a particular equalization practice is lawful the Commission looks "to the economies" and the "natural flow of commerce." Thus where the berth facilities of two or more ports are located in and serve one area, a distinction is made between that case and the case where the facilities are located in, and serve, different geographic areas.

Port Comm. of Beaumont v. Seatrain Lines,
2 USMC 500; (1941)

Port Comm. of Beaumont v. Seatrain Lines,
2 USMC 699; (1943)

Beaumont Port Commission v. Seatrain Lines, Inc.,
3 FMB 566; (1951)

In City of Portland v. Pacific Westbound Conference, 5 FMB 118, the Commission found certain equalization practices of the Conference unlawful but it also found that equalization practices on explosives from Dupont, Washington were justified because of inadequacy of direction steamship service to the

Philippines and would continue to be justified until direct monthly sailings were provided. The two orders referred to above were reviewed by the Appellate Court in Pacific Far East Line, Inc. v. U.S., 246 F(2d) 711 (1957) and were upheld.

To find equalization unlawful, the Commission must first find a violation of law. As the decision points out, contrary to Stockton's position, the equalization practice approved by the Commission does not violate sections 16 and 17 of the Shipping Act because the discrimination and prejudice prohibited under those sections is discrimination which is unjust and unreasonable. Differences in treatment based on valid reasons are not violations of the Shipping Act. (West Indies Fruit Company v. Flota Mercante Grancolombiana, 47 FMC 66 (1962).

The basis of the Commission decision is that equalization is a proper device where the cargo being equalized comes from territory tributary to the port of loading. What is tributary depends on the facts of the particular case. It includes not only geographic considerations but such other criteria as frequency of service. The whole basis of Stockton's objection lies in its concept, which finds no support whatever in law, that cargo cannot be tributary to more than one place of loading. Contrary to what Stockton asserts, the Commission did not place Stockton on the shore of the Golden Gate but it

did find that the entire flow of ocean traffic from the entire geographical area was to the Pacific Ocean via the Golden Gate. (FMC Dec., p. 11; R. 1276.) The concurring opinion correctly points out that a carrier servicing Stockton must pass San Francisco at least twice. Therefore if Stockton is served, San Francisco is served. (FMC Dec., p. 19; R. 1284.)

Stockton has an ingenious theory of tributary territory which we have outlined in our statement of facts, infra. (See R. 1279.) If Stockton were correct, there would be no reason for the Commission to ever determine tributary territory since the determination would be a mere mechanical exercise. Obviously, Congress intended no such result when it directed the Departments of Commerce and Defense, pursuant to Section 8 of of the Merchant Marine Act, 1920 "to investigate territorial regions and zones tributary to . . . ports, taking into consideration the economies of transportation by rail, water and highway and the natural direction of the flow of commerce;" (46 U.S.C. 867.) Exhibits 47 to 50 in this record show the findings of the Maritime Administration in connection with territory tributary to Sacramento, Stockton, San Francisco, Oakland and Alameda. The conclusion of the Federal Maritime Commission in this case is consistent with those findings.

III

STOCKTON'S ALLEGED "SPECIFICATIONS OF ERROR" ARE FALLACIOUS

The brief of the Pacific Westbound Conference sets forth each alleged basis of error and conclusively refutes its validity. To avoid unnecessary repetition, this intervenor adopts the arguments made by the Conference. (See PWC Brief, pp. 6-9.)

Concisely, we agree there is no showing of a violation of Section 8 of the Merchant Marine Act, 1920, (46 U.S.C. 867). Stockton bases a portion of this argument on the principle that equalization is a "rebate." Equalization is not a rebate. No profit accrues to the shipper or to the owner of the goods. All a carrier does when equalizing is to pay, itself, that portion of the inland transportation cost between the closest port of loading and the port of loading which the carrier for its own convenience elects to use. Nothing in Section 8 prevents this.

Section 205 of the Merchant Marine Act, 1936, (46 U.S.C. 1115) assures that there will be no rate discrimination. There is no rate discrimination. This section does not prohibit equalization.

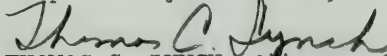
Stockton's remaining arguments, based on the theory that equalization affords a rebate, are are incorrect and unsound. This is not a rebate case.

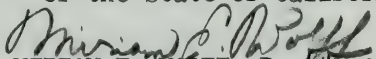
The last argument of Stockton that there is a violation of the Fifth Amendment of the Constitution is incorrect because it is based on the principle that Stockton has a property right in the cargo it alleges should move through Stockton. This is not true and is effectively dissipated in the brief of the Conference (PWC Brief, p. 49) and in our discussion, infra, showing the cargo, in fact, remains tributary to San Francisco.

CONCLUSION

We respectfully petition the decision of the Federal Maritime Commission be affirmed.

Respectfully submitted,


THOMAS C. LYNCH, Attorney General
of the State of California


MIRIAM E. WOLFF, Deputy Attorney
General of the State of California

Attorneys for Intervener,

STATE OF CALIFORNIA

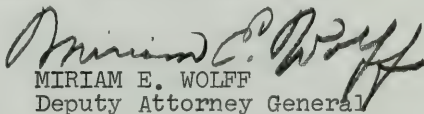
Dated: San Francisco, California, August 12, 1966

Certificate of Counsel and of Service

I certify that, in connection with the preparation of this brief, I have examined Rules 18 and 19 of the United States Court of Appeals for the Ninth Circuit, and that, in my opinion, the foregoing brief is in full compliance with those rules.

I further certify that I have this day served the foregoing document upon all parties of record in this proceeding by mailing, postage prepaid, a copy to Honorable Nicholas deB. Katzenbach, Attorney General of the United States, attention of Irwin A. Seibel, and a copy to Federal Maritime Commission, attention of Walter H. Mayo III, attorneys for the respondents; a copy to James L. Pimper, General Counsel, Federal Maritime Commission; a copy to Albert E. Cronin, Jr. and J. Richard Townsend, attorneys for the petitioner; a copy to Leonard G. James, attorney for interveners Pacific Straits Conference and Pacific/Indonesian Conference and member lines; and a copy to Lillick, Geary, Wheat, Adams & Charles, attention of Gordon L. Poole, attorneys for Pacific Westbound Conference and members.

Dated at San Francisco, California, August 12, 1966.


MIRIAM E. WOLFF
Deputy Attorney General

Attorney for Intervener,
State of California

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No. 20544

In the

United States Court of Appeals

For the Ninth Circuit

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Petitioner,

vs.

FEDERAL MARITIME COMMISSION AND UNITED
STATES OF AMERICA,

Respondents.

Brief of Intervenor

Pacific Westbound Conference and Its Member Lines

FILED

AUG 12 1966

WM. B. LUCK, CLERK

EDWARD D. RANSOM

GORDON L. POOLE

LILICK, GEARY, WHEAT, ADAMS
& CHARLES

311 California Street

San Francisco, California 94104

*Attorneys for Intervenor Pacific
Westbound Conference and
Its Member Lines*

Dated: August 11, 1966

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I.

INTRODUCTORY

A. Counterstatement of the Case

Petitioner's "Statement of the Case" (Stock. Br. 2-7)¹ is an irrelevant reiteration of the contentions resolved against Stockton by the Presiding Examiner and the Federal Maritime Commission

1. Throughout this brief, the following abbreviations will be employed: "Stock. Br." for Petitioner's Opening Brief, "Com. Rep." for the Commission's Report and Order, "Concur. Op." for Commissioner Patterson's Concurring Opinion, "I.D." for the Presiding Examiner's Initial Decision, "Tr." for the Reporter's Transcript of Testimony and "R." for the Record of this Court.

rather than a description of issues properly before this court upon review of the final action of an administrative agency. The obvious intent of Stockton throughout its brief is to invite this court to substitute its judgment for that of the Commission with respect to fact, law and policy matters, which Congress has entrusted to the agency expert in the maritime regulatory field for final determination in the exercise of its functions under the Shipping Act, 1916. On judicial review of the agency action, the issue is not whether other findings and conclusions were permissible, but rather whether it is warranted by the record and has a reasonable basis in law; a test plainly met here.

In any event petitioner's Statement of the Case is incomplete and misleading calling for an introductory counterstatement of the principal issues of the case.

For approximately twenty-five years the Pacific Westbound Conference (PWC) and its member lines serving the outbound trade from the Pacific Coast to the Orient have practiced port equalization in the San Francisco Bay Area with the approval of and in accordance with standards laid down by the Commission and its predecessor agencies (Tr. 758, 771-75). Simply stated, that practice affords to shippers located closest to terminal ports, which do not have service adequate to meet their needs, access to vessels loading at other terminal ports at no additional cost to the shipper and at the least cost to the carrier. This is accomplished by having the carrier absorb the difference in inland transportation costs between shipping to the terminal port located nearest to the shipper and the costs of shipping via the terminal port more distant from the shipper but, as to the shipment equalized, more convenient to the carrier's operation.

There is no serious dispute over the fact that equalization is beneficial to the shipper and that the shippers who use it are enthusiastic supporters of equalization as is fully documented at pages 23-25, *infra*. Access to frequent and dependable service enables the shipper to be competitive with his domestic and

foreign competitors and increases and is beneficial to the foreign commerce of the United States.

As we will show subsequently (*infra*, pages 21-23), equalization is also undeniably beneficial to the carrier in enabling it to make the most efficient and economic use of its vessels. Without equalization, carriers would be forced to one of three costly alternatives on nearly every sailing: either, (1) proceed to each terminal port to pick up minimal parcels of cargo, an uneconomic trip, or, (2) transship from one port to another by truck or barge at carriers' entire expense plus the charges of two terminal operators, i.e., the nearest port and the port where the cargo is loaded, or, (3) forego the cargo. When carriers' costs are increased the addition can only come from corresponding increases in ocean rates. Elimination of equalization would seem to make freight increases inevitable.

Stockton competes with its sister ports in the San Francisco Bay Harbor Complex for the industrial and agricultural exports originating in Northern California. No other port has attacked equalization and one port, San Francisco, intervened in the proceedings on behalf of the ocean carriers and demonstrated that its interest in equalization was at least equal to that of Stockton (Tr. 1134-35, 1143-45). The abandonment of equalization could only come at the expense of San Francisco and other Bay Area ports competitive with Stockton. Equalization has no effect upon Stockton's principal activity—the handling of bulk cargoes. (Exs. 44-46; Tr. 144). If the Commission decision, upholding equalization between the San Francisco Bay Harbor Complex ports, is reversed, the segment of the foreign commerce of the United States served by those ports would be impeded.

The policy question determined by the Commission was whether the narrow self-interest of an individual port, Stockton, must prevail over the combined interests of shippers, carriers and Stockton's sister ports in the Bay Area which serve tributary areas overlapping or identical with Stockton's tributary area. The Fed-

eral Maritime Commission held that the foreign commerce of Northern California should not be fragmented arbitrarily into blocks of cargo which become the monopoly of individual ports, each of which serve the same geographical area, to the point where shipper needs are ignored, efficient and economical steamship service is compromised and the foreign commerce of the United States inhibited. The question now before this Court is whether that policy and the findings and determinations leading up to that policy determination are reasonably supported by the record and are warranted by law.

B. Spurious Issues Raised by Stockton

In its Statement of the Case, Stockton raises several spurious issues. For example, at page 2 of its brief Stockton contends that the decision of the Commission will have "a far-reaching, disastrous effect" on various ports throughout the United States. If this were a valid observation many ports might have been expected to intervene. It is just not so and this is a blatant attempt to inflate the localized findings and conclusions of the Commission into a matter of national significance.

The issues in this case and the Commission report and decision deal only with certain California ports. This appeal concerns only that portion of the decision relating to those ports serving Northern California's hinterland located on the waterways served through the Golden Gate—the San Francisco Bay Harbor Complex Ports. There was not one shred of evidence concerning ports or ocean carrier service outside California or any possible effect of equalization upon the same.

The contention that, through equalization the Conference Lines "and indeed foreign steamship lines" have the power to determine which ports shall prosper and which shall be deprived of cargo, is another unwarranted charge. As more fully demonstrated below (*infra.* pages 17-28), the Commission's conclusions that equal-

ization is justified rest upon geographical, economic and public interest considerations above and apart from any claimed but non-existent desire of the respondent carriers, irrespective of nationality, to encourage or stifle port development.

The suggestion consistently intimated, but never documented, that, through equalization, Stockton has suffered any decline of its fortunes as a port is wholly unsupported in view of the uncontradicted evidence showing Stockton has continued its astonishing growth as the self-advertised "West Coast's fastest growing port" during the years it has supposedly been disadvantaged by equalization (Tr. 144). Unlike the other ports within the San Francisco Bay Harbor Complex with which it competes, Stockton has enjoyed enormous gains in the amount of cargo of every description handled by it since its designation by the Conference as a terminal Port in 1957 (Exs. 44-46).

The attention of this Court should also be directed to the persistent reference by Stockton to equalization as a "rebate." That term, as we shall see, when used in connection with Section 16(Second) of the Shipping Act, 1916, (46 U. S. Code 815) (the alleged basis for Stockton's use of the term) connotes payments made surreptitiously and unfairly to a shipper, so as to give him a rate lower than that provided for in the published tariff. During the course of the proceedings Stockton charged that equalization is a "cloak for malpractices" and that equalization payments were improperly calculated under the tariff rules. All such contentions were resoundingly rejected, both by the Examiner and the Commission, (Com. Rep. 17-23, I.D. 21-26; R. 1282-88, 1252-57) and no objection to that part of the decision is taken to this Court. The persistent recourse by Stockton to the term "rebates" serves no legal purpose and its use is obviously intended solely for its inflammatory effect.

SUMMARY OF ARGUMENT²

A. That Courts will not substitute their judgment for that of an administrative agency and that the findings of such agencies are entitled to great weight, are well recognized principles of law. Their application to decisions of the Federal Maritime Commission, which possesses expertise in the field of shipping regulation, has been most recently recognized in *Consolo v. Federal Maritime Commission*, *infra*, at page 12, and by this Court in *Trans-Pacific Freight Conference of Japan v. Federal Maritime Commission*, *infra* at page 11. In the instant case the Commission and the Examiner before it, after an extensive hearing, prepared thoughtful, logical decisions fully supported by findings and conclusions. The Petitioner, Stockton Port District, therefore has the heavy burden of making a clear and convincing showing of alleged errors. Stockton has failed to discharge that burden, but instead improperly seeks to have this Court substitute its judgment for that of the Commission.

B. The Commission and the Examiner both concluded that the Port of Stockton should properly be considered an integral port of and within the San Francisco Bay Harbor Complex and that areas naturally tributary to Stockton are equally so to, and can be naturally served at, San Francisco and the other ports within the same geographical area. These conclusions were made after the Commission and Examiner had considered all factors bearing upon the economics of transportation and the natural flow of traffic through San Francisco Bay and connecting waterways to the Far East. These included the close geographical relationship between the ports served through the Golden Gate and the historical pattern of the successive development of the San Francisco Bay Harbor Complex ports, each competing for cargoes originating in the same or overlapping tributary territory. Also

2. Provisions of statutes and regulations relied upon by these intervenors in support of their position appear in Appendix A of this Brief.

weighed were the economics of ocean carriers for whom consolidation of loading operations is necessary to promote efficient service and the shipping public who need equalization to give them access to the shipping services they would not otherwise have and which is vitally needed to enable them to compete effectively in world markets. The Commission and the Examiner also duly considered prior determinations made by the Departments of Commerce and Defense, and the State of California, which in full accord with the Commission's conclusions, recognizes the unity of the San Francisco Bay Harbor Complex Ports. The findings and conclusions of the Commission in this regard are fully supported by substantial evidence.

C. Section 8 of the Merchant Marine Act, 1920, (46 U.S.C. § 867) is evidence of a Congressional policy favoring port development. No functions under that statute have been transferred to the Federal Maritime Commission. The Commission, nonetheless, gave full consideration to the policy evidenced by Section 8 in concluding that the ports on San Francisco Bay and connecting waterways all serve the same tributary area. In an attack on the Commission, in which reason is dethroned, Stockton inaccurately accuses the Commission of "ignoring" the policy of Section 8 while at the same time castigating the Commission for implementing that policy by acting in accordance with definitive reports of the Departments of Commerce and Defense prepared pursuant to Section 8, respecting the San Francisco Bay Harbor Complex Ports.

D. The Commission carefully weighed equalization in the light of the public interest, which includes each participant in the overseas commerce of Northern California—the shipping public who need and require equalization, and the ocean carriers, to whom equalization is an economic necessity. The Commission also considered other participants, the interests of the ports, finding that Stockton's claims of lost cargo and lost revenues were overstated and speculative and that cessation of equalization

could only come at the expense of Stockton's sister ports in the same geographical area. The Commission concluded, on the basis of these facts, that equalization was beneficial to the foreign commerce of the United States and in the public interest. Stockton insists that the public interest, as a matter of law, is identical with the self-interest of Stockton and that the other interests can not properly be considered, a proposition unsupported by the facts, logic, by Section 8 of the Merchant Marine Act, 1920, or otherwise by law.

E. The Commission found that, since all the ports on San Francisco Bay and its connecting waterways are in the same geographical area, and each naturally serves the same tributary area, the prejudice or disadvantage, if any, to the Port of Stockton arising from equalization was neither unjust, undue or unreasonable within the meaning of Sections 15 and 16 (First) of the Shipping Act, 1916 (46 U.S.C. §§ 814, 815). This conclusion is also supported by the Commission's findings that equalization is in the public interest by promoting the interests of shippers and carriers. Stockton is unable to demonstrate it has exclusive claim to cargoes originating in the San Joaquin Valley, or that it has a legal right to such cargo superior to the interests of its sister ports, the shippers and carriers. Stockton's claim that Sections 15 and 16 (First) require adoption of its unsound, constructive mileage theory of port cargo control has no basis in law. The findings and conclusions of the Commission respecting the lack of undue, unjust or unreasonable discrimination or prejudice, being supported by substantial evidence, are clearly warranted by law.

F. Stockton's claim that the Commission's Report and Order is inconsistent with prior decisions is not a valid basis for setting aside the later decision of an administrative agency. The question is whether the Commission's decision has support in the record and is in accordance with law. Nonetheless, the Commission report and order represents a painstaking and successful effort to

reconcile its decision in this case with its prior decisions and those of its predecessor agencies. Stockton's efforts to distinguish these cases are wholly unavailing.

G. Section 205 of the Merchant Marine Act, 1936, (46 U.S.C. § 1115) is administered, not by the Commission, but by the Department of Commerce acting by and through the Maritime Administration. The policy lying behind the statute is to assure that service will not be prevented at ports constructed with federal funds by rate discrimination, whereby carriers assess different ocean rates at such a port than at an adjacent port. The carriers here are in literal compliance with that policy since the same ocean rates, and (if pertinent to Section 205) the same equalization rules apply at every San Francisco Bay Harbor Complex terminal port. In any event equalization does not prevent service at Stockton, but enables carriers to compete for Northern California cargoes on an economically feasible basis, a result not contrary to any policy derived from Section 205.

H. Section 16 (Second) of the Shipping Act, 1916, (46 U.S.C. § 815) makes it a criminal offense for a carrier, by means of concealment and falsification or other unjust or unfair means, to charge any shipper less than as provided in its established and published rates. Stockton, in a newly discovered claim, charges the carriers with violation of Section 16 (Second) despite the Commission's clear rejection of comparable charges against equalization made by Stockton under other provisions of law. Stockton's claim in this regard rests upon a distorted reading of the equalization rules provided in the Conference tariff and is entirely without merit.

I. Stockton's casual claim of a violation of the Fifth Amendment of the United States Constitution is wholly without substance, particularly since the Commission's Report and Order is warranted by law and supported by substantial evidence.

ARGUMENT**A. Scope of Judicial Review**

The standards applicable to this judicial review are found in Section 10(e) of the Administrative Procedure Act (APA), (5 U.S.C. § 1009(e)). It has been explained that:

"The provisions of Section 10 constitute a general restatement of the principles of judicial review embodied in many statutes and judicial decisions. . . .

"This [Section 10] restates the present law as to scope of judicial review." (Attorney General's Manual on the Administrative Procedure Act, 1947, pp. 98 and 108.)

Section 10 provides that the court of review shall set aside agency action, findings and conclusions in six different situations. Stockton has, in its Petition for Review (Par. IX) invoked 3 of the 6 grounds for review (under subparagraphs (1), (2) and (5) of Section 10(e)(B)). Petitioner asks this Court to review the Report and Order to determine whether it has shown the Commission's decision to be "arbitrary, capricious, an abuse of the Commission's power of discretion, and not in accordance with law, . . . unsupported by substantial evidence . . . and is to such extent based on errors of law" and whether it "deprives petitioner of property without due process of law in violation of the Fifth Amendment . . ."³

Resolving considerations under the Shipping Act, 1916, as amended, is a complex task which requires expert judgment and considerable knowledge of the shipping industry. Congress gave that task to the Federal Maritime Commission (Reorganization Plan No. 7 of 1961, 46 U.S.C. § 1111 (note)). This court

3. Stockton makes no claim that the Commission acted in excess of its statutory jurisdiction, authority or limitations or short of statutory right, or without the observance of procedure required by law (Sec.10(e)(B)(3) and (4)). This is not a case where the courts review facts *de novo* referred to in Sec. 10(e)(B)(6).

has recognized the discretion confided to the Commission in administering those regulatory acts entrusted to it.

"It has long been recognized that (the Commission) . . . has a broad discretion in effectuating the policies of the (Shipping) Act. . . . The question always is whether the determination . . . has 'warrant in the record' and a 'reasonable basis in law'. . . .

"* * * * Unless it be recognized that the Commission had this discretion and power of determination it could not be said to have adequate power to effectuate the policies of the Shipping Act." *Trans-Pacific Freight Conference of Japan v. Federal Maritime Commission*, 314 F.2d 928, 935 (9th Cir. 1963).

The burden is on Stockton to demonstrate to the Court why any findings or conclusions of the Commission should be rejected and that other findings and conclusions must be made. "[H]e who would upset the . . . order under the Act carries the heavy burden of making a convincing showing that it is invalid because it is unjust and unreasonable in its consequences" (*Interstate Commerce Commission v. Jersey City*, 322 U.S. 503, 512-13 (1944)).

The role of the agency is described by the Supreme Court as follows:

"We think the court misconceived not only the effects of the Commission's action in these cases but also its own function. It is not true, as the opinion stated, that '. . . the courts must in a litigated case, be the arbiters of the paramount public interest.' This is rather the business of the Commission, made such by the very terms of the statute. The function of the reviewing court is much more restricted. It is limited to ascertaining whether there is warrant in the law and the facts for what the Commission has done. Unless in some specific respect there has been prejudicial departure from requirements of the law or abuse of the Commission's discretion, the reviewing court is without authority to intervene. It cannot substitute its own view concerning what should be done, whether with reference to competitive considerations

or others, for the Commission's judgment upon matters committed to its determination, if that has support in the record and the applicable law." (*United States v. Pierce Auto Freight Lines*, 327 U.S. 515, 535-36 (1946).)⁴

Section 10(e) has been interpreted by the Supreme Court to require a reviewing court to affirm the findings of an administrative agency if, taking the record as a whole, they are supported by substantial evidence. In a recent decision the Supreme Court defined its role in this regard as follows:

"We have defined 'substantial evidence' as 'such relevant evidence as a reasonable mind might accept as adequate to support a conclusion.' . . . '[I]t must be enough to justify, if the trial were to a jury, a refusal to direct a verdict when the conclusion sought to be drawn from it is one of fact for the jury.' . . . *This is something less than the weight of the evidence, and the possibility of drawing two inconsistent conclusions from the evidence does not prevent an administrative agency's finding from being supported by substantial evidence.* . . .

"Congress was very deliberate in adopting this standard of review. It frees the reviewing courts of the time-consuming and difficult task of weighing the evidence, it gives proper respect to the expertise of the administrative tribunal and it helps promote the uniform application of the statute." (*Consolo v. Federal Maritime Commission*, U.S., 16 L.ed 2d 131, 140-1 (1966) (Citations and footnotes omitted)).

In matters of statutory construction, the Court will give great deference to the interpretation given the statute by the officers or agency charged with its administration. *Udall v. Tallman*, 380 U.S. 1, 16 (1965); *Pennsylvania R. Co. v. Day*, 360 U.S. 548, 552 (1959). In *Udall v. Tallman* the Court restated the role of the Courts and Agencies in construing the statutes as follows:

⁴ Emphasis throughout this Brief supplied unless otherwise noted.

" 'To sustain the Commission's application of this statutory term, we need not find that its construction is the only reasonable one, or even that it is the result we would have reached had the question arisen in the first instance in judicial proceedings.' " 380 U.S. at 16. (Citations omitted).

Throughout its brief petitioner relies almost exclusively upon extensive quotes from the dissent of Commissioner Hearn, who alone of the five Commissioners disagreed with the findings and conclusions of the Examiner. The court, however, is in no way bound by this dissent, and its existence cannot be considered grounds for reversal of the Commission's order. The Commission "acts as a unit, and a dissent no more reduces the legal effect of its findings and orders than does a dissenting opinion of a member of a court detract from the legal effect of the court's judgment." *Sperry Gyroscope Co. v. N.L.R.B.*, 129 F.2d 922, 924 (2d Cir. 1942).

"The fact that differences of opinion regarding the facts and the law existed within the Commission and its staff does not, of course, mean that the final order of the Commission is entitled to any less respect than it would possess had the issues been decided unanimously." *United States v. I.C.C.*, 198 F.2d 958, 963 fn. (D.C. Cir. 1952).

The validity of the Commission's action does not depend upon unanimity among agency members, but upon compliance with the criteria set forth in Section 10(e) of the APA. *United States v. I.C.C.*, *supra*; *Wyman Gordon Co. v. N.L.R.B.*, 153 F.2d 480, 483 (7th Cir. 1946); *N.L.R.B. v. Murray Ohio Co.*, 326 F.2d 509 (6th Cir. 1964).

On the other hand, additional weight should be given to the fact that the Commission's Report and Order, and Commissioner Patterson's concurring opinion specifically incorporate the Initial Decision of the experienced Presiding Examiner who heard and weighed the evidence presented before him in the first instance, as follows:

"For the reasons set forth herein we agree with the conclusions of the examiner and, if in stating those reasons we fail to treat any 'specific exception', it has nevertheless been considered and found not justified." (Com. Rep. 10, R. 1275; See also Concur. Op. 8, 9, 11, 12, 19, 20; R. 1313-14, 1316-17, 1324-25).

The Commission considered and rejected a barrage of exceptions to the Examiner's Initial Decision, many of which have been renewed here. Petitioner's claims have thus been found wanting at both levels of the administrative process.

While Stockton claims "arbitrariness, capriciousness, and abuse of discretion" it does not argue these points. Such claims have been held to be wholly without merit when an agency makes sufficient findings to be dispositive of the statutory issues. *Baltimore Transfer Co. v. I.C.C.*, 114 F.Supp. 558, 564, *aff'd* 346 U.S. 890 (1953).

The foregoing legal principles must be kept constantly in mind in considering petitioner's brief for it makes no effort to direct its arguments within the legal principles governing the scope of judicial review. Essentially its arguments are an appeal to this Court to disagree with the agency as to findings and conclusions lawfully drawn by the Examiner and Commission in the exercise of their respective expertise and authorized discretion. Petitioner, contrary to the standard so recently reiterated by the Supreme Court in *Consolo, supra*, appeals to this Court to make *other* and inconsistent findings and conclusions from those made by the Commission.

B. The San Francisco Bay Harbor Complex Ports

1. THE COMMISSION'S FINDINGS AND CONCLUSIONS.

There are 16 terminal ports served by the PWC stretching along the Pacific Coast of the United States and Canada from Vancouver, B.C., southward to San Diego. Terminal ports are those designated by the Conference as to which the same ocean rates shall apply (Ex. 1c). There are an extraordinary number of ports

located on San Francisco Bay and its connecting waterways—the San Francisco Bay Harbor Complex. Inside the Golden Gate are 16 ports including six PWC terminal ports (San Francisco, Oakland, Alameda, Richmond, Stockton and Sacramento), the largest concentration of terminal ports on the Coast (Exs. 1c, 4, 60).

The Commission held: "We agree with the examiner's conclusion that the ports of Stockton and San Francisco do not represent separate and distinct geographical areas." (Com. Rep. 12, R. 1277). The Examiner's conclusion referred to described the unifying geographical features of these ports as follows (I.D. 14, R. 1245):

"As between Stockton and San Francisco, with which this proceeding is chiefly concerned, we are not dealing with ports of a given geographical area versus those of another geographical area, but with a single port as against another port in the same geographical area—in fact, in the same harbor complex. In a geographical sense, both ports, together with the other ports on the San Francisco bays and their connecting waters, may be described as San Francisco bay ports. . . . The natural direction of the flow of ocean traffic from the entire relevant geographical area is to the Pacific Ocean via the Golden Gate; that strait is the ocean portal through which ocean traffic to and from the harbor or haven must flow. Stockton simply does not exist as an ocean port separate from the Golden Gate and the San Francisco bays."

Commissioner Patterson, in his Concurring Opinion (p. 19, R. 1324) stated that the foregoing statement of the Examiner,

"... serves the useful purpose of highlighting the dominating geographical fact of this case, and of recognizing the geographical fact which prevents Stockton from having superior rights over San Francisco. The fact is that, to serve Stockton once, a carrier must go through the Golden Gate and pass San Francisco at least twice. If Stockton is served, so inevitably is San Francisco."

The Commission also found, in addition to the common bond of the geography:

"The natural direction of the flow of traffic from the San Joaquin Valley, which Stockton seeks to have declared its exclusive preserve, is through the Golden Gate to the Pacific Ocean. For almost a hundred years before Stockton was made accessible to oceangoing vessels, San Francisco was the principal port through which freight from the San Joaquin Valley would and did pass. It did not cease to be such a port merely upon the creation of an additional port at Stockton." (Com. Rep. 13, R. 1278).

The Commission adopted the following conclusion, as did the Examiner (I.D. 19, R. 1250), in the following language:

"We conclude, that for the purposes of this proceeding, the territory naturally tributary to Stockton should properly be considered naturally tributary to San Francisco and other San Francisco Bay area ports. To paraphrase the *Beaumont* decision, *supra*, the territory surrounding Stockton and the entire Bay area is centrally, economically and naturally served by the conference facilities at San Francisco." (Com. Rep. 16, R. 1281).

At page 20 of his concurring opinion (R. 1325), Commissioner Patterson interpreted and commented on this conclusion as follows:

"I understand the Examiner to be saying in effect that detriments to commerce have to take this dominating fact into consideration, (i.e., the common Gateway of the Golden Gate) and the measuring point for territory 'naturally' tributary or the point where the 'natural' flow ends is not Stockton, but the Golden Gate. Unless carriers and shippers can avoid San Francisco by going to Los Angeles or somewhere else on the Pacific Coast, they should be able to make the most efficient arrangements possible to get cargo past the Golden Gate."

2. SUBSTANTIAL EVIDENCE SUPPORTING THE FOREGOING FINDINGS AND CONCLUSIONS.

Stockton argues (Stock. Br. 27-37) that the foregoing findings are unsupported by substantial evidence. The considerable evidence and factors considered by the Commission and the Examiner in this regard are outlined in the "Facts" (Com. Rep. 2-9, R. 1267-74) and "Background Facts" (I.D. 4-6, R. 1235-37) of their respective decisions, as well as in the discussion of the same. The evidence considered by the Commission may be summarized as follows:

a. Geographical Considerations

The logical first step taken by the Commission was to analyze, from the ocean transportation point of view, the salient geographical features of the San Francisco Bay Harbor Complex Ports. Of first importance, the "dominating geographical fact" of this case (Concur. Op., 19, R. 1324) and one obvious from the map (See, Ex. 60), is that the Golden Gate serves as the doorway to extensive protected navigable waterways reaching inland into Northern California's hinterland. This unique natural harbor system serving Northern California is well known to this Court. The large number of ports sharing this common gateway located on San Francisco Bay, and its connecting waterways include the 6 terminal ports with which we are here particularly concerned (San Francisco, Oakland, Alameda, Richmond, Stockton and Sacramento).

A vessel calling at Stockton or Sacramento passes twice by the "front door" of Oakland, Alameda or Richmond. Vessels calling at any of the Harbor Complex Ports necessarily call at or pass through or within hailing distance of the Port of San Francisco. This unifying feature, i.e., the common ocean gateway and the series of connecting deepwater waterways must be kept constantly in mind in view of Stockton's attempts to obscure this geographical relationship.

Stockton at page 37 of its brief ridicules the Commission for asserting that Stockton and San Francisco are in the same geographical area by ripping the term "geographical area" out of context and calling it "meaningless". However, when the Commission's predecessor used the same term in *City of Portland v. Pacific Westbound Conference*, 4 FMB 664, 679 (1955) a case which Stockton professes to admire, no such exception is taken to the use of the phrase (Stock. Br. 39).

Stockton vigorously contests the description of Stockton as a "San Francisco Bay" or "Bay Harbor Complex Port" relying principally upon captious comments, echoing those of the dissenting Commissioner, intimating that the Commission has crudely remade the map of Northern California. The Commission is charged with "transposing" Stockton to the shores of San Francisco Bay, a charge superficially bolstered by various exercises such as reciting the mileage between the Golden Gate and Stockton, the names of the various subsidiary bays and channels traversed by vessels proceeding to Stockton and distinguishing the San Joaquin Valley from San Francisco Bay (Stock. Br. 29-30). Such efforts miss the mark because they are not directed to relevant factors—the economics of transportation and the natural flow of commerce.

b. Port Development in the S. F. Bay Harbor Complex

(1) Historical Growth

The first port facilities in the San Francisco Bay Area were established at the Port of San Francisco, which enjoys, as noted above, among other natural advantages, the first suitable port location inside the Golden Gate. San Francisco was the first port established in 1863 by the California State Legislature as a harbor for the commerce of the entire State (Tr. 1114-20, 1131-32).

Subsequently, deep water ports were established at Oakland and Alameda on the eastern shore of San Francisco Bay opposite

San Francisco. Somewhat later the Port of Richmond was developed on the eastern shore near the northern extremity of San Francisco Bay. There are a dozen or more additional ports or facilities located on the Bay or on connecting waterways to the Bay. Leading from the Bay southeasterly on the San Joaquin River and served by the Stockton deepwater channel is the Port of Stockton, 75 nautical miles from the Golden Gate. Initial construction of that waterway commenced in 1933 and Stockton was recognized as a terminal port in 1957. Sacramento, the most recently established port (it became a PWC terminal port in 1963) for ocean-going vessels, is located on the Sacramento River, about 80 nautical miles from the Golden Gate. (Ex. 4, 60; Tr. 877, 1114-16).

As the San Francisco Port Authority Director testified, all the foregoing ports including San Francisco and Stockton have been competitive for 35 years (Tr. 1129-32). Each new port upon its creation has entered the competition for Northern California cargoes.

(2) The Complementary Roles of the Ports

Further demonstration of this unitary concept—the inter-relationship of the ports—was shown by the complementary roles each play in Northern California's ocean-borne commerce. As the Director of the Port of San Francisco testified:

“We are talking about a large basin, so to speak, and I think that ports . . . within that area should be considered as one group rather than as an individual port against port. . . .” (Tr. 1132).

San Francisco has by far the greatest variety and number of berths, piers, and other facilities served by no less than one hundred sixty-eight steamship lines. It has for many years been the primary general cargo port of the area (Tr. 1114-20, 1131-32). The East Bay ports of Oakland and Alameda, also are primarily general cargo ports with heavy emphasis on canned goods. San Francisco,

Oakland and Alameda tend to be, therefore, the last ports of loading outbound, and the first ports to discharge cargo homebound, for general cargo vessels.

Richmond, another Bay Area terminal port, handles largely bulk cargoes, scrap and petroleum products along with some general cargo (Tr. 1115). Sacramento has not been operational very long as a deep water port, although it seems logical to assume that it, like Stockton, will develop as an important bulk cargo port for commodities like rice (Tr. 149-51). The other non-terminal ports of the region on San Francisco Bay proper, Suisun Bay, San Pablo Bay, serve specialized roles such as ores (Selby) or petroleum in tankers (Avon and Martinez). A number are private ports catering largely to the shipments of the proprietors of the ports. Others, like Redwood City, are non-terminal public ports (Tr. 1111-16).

Stockton also has its special niche in this ocean-borne commerce complex. The record contains a statistical record of the cargo handled by the Port of Stockton. In 1962, a little over three-quarters of all export cargoes moving through Stockton were made up of bulk or bottom cargoes (Ex. 46).⁵ Thus, Stockton *is basically a bulk cargo or bottom cargo port* though it does handle exports of a general cargo nature though, as we shall show in the paragraphs which follow, not in significant amounts in the transpacific trade here involved.

(3) Traffic Originating at Stockton

The amount of service provided by PWC vessels at Stockton is governed principally by offerings of bottom cargoes—grains, fertilizers, seeds, ores and the like—moving to Far East destinations. (Tr. 768-70, 872-73, 121-23, 166). They are loaded and shipped sporadically in sizeable parcels in excess of 1,000 tons (Tr. 880-

⁵ During the hearing bottom cargo was identified as cargoes loaded in bulk or the same lower rated commodities (moving in sizeable lots) in bags. Commercial general cargo is essentially packaged cargo moving in relatively small lots and includes all cargo other than bottom and military cargo (Tr. 768-69, 880-81, 888-89).

81). These offerings are not spaced with the regularity to justify regular service by PWC cargo liner vessels at Stockton (Tr. 491, 881, 1059-61, 1074, 1083-84).

There are relatively small offerings of a general cargo nature moving from Stockton to the Far East—mostly condensed milk, raisins, nescafe, hides and lumber. As Commissioner Patterson observed (Concur. Op. 23, R. 1328):

“The uneconomic nature of cargo available at Stockton is shown by the fact that the commodities affected by equalization rules average 40 tons per shipment, and in 1961 71% of all Trans-Pacific Conference ships calling at Stockton loaded as little as from 0-50 tons of general cargo per departure (Exh. 52)” (See Exs. 11, 13; Tr. 968-69).

c. Transportation Economics

(1) The Ocean Carriers

The PWC carriers serving the Orient through the Golden Gate call at San Francisco, Oakland or Alameda on 85-90% of the total Conference sailings, usually as the last port, because general cargoes are concentrated there (Tr. 765-66, 793-95). While Conference vessels do call at Stockton (84 and 133 calls in 1962 and 1963, respectively), such service is sporadic and irregular (Ex. 56; Tr. 138, 771). Some calls are made attendant with the need to discharge cargo coming inbound, many others are made to load outbound bulk or bottom cargoes. Such vessels do not attract general cargoes destined outbound to the Far East because they generally proceed elsewhere to continue discharging and loading operations for 10-12 days after leaving Stockton and this conflicts with shipper desires for prompt and rapid dispatch of their cargoes to their ultimate Far East destinations. Little general cargo is attracted (Tr. 469-70, 490, 513, 873).

In order to load general cargo at Stockton vessels must frequently shift from bulk loading and discharging berths, to another pier suitable for general cargo at a cost of \$300 per shift placing

an effective minimum upon the amount of cargo sufficient to justify the shift. Depending on commodity, this varies from 250 to 700 tons (Tr. 873-76, 493).

Further, the economic cost of calling Stockton was considered by the Commission. The round trip from San Francisco to Stockton involves an extra expenditure of \$3200-5000 (Tr. 531-35, 877, 1083, 1101-2). Quite obviously the carrier cannot undertake expenditures of this magnitude without the prospect of adequate cargo revenue to justify the call.

Consolidation of cargo operations at a lesser number of ports is obviously an important means of controlling the ever increasing vessel costs of the Conference member lines (Tr. 886-7, 1086). From a steamship operating standpoint unnecessary multiple port loading in any given area means an economic waste. This is particularly so in the case of vessels which arrive at the Golden Gate for "top off" loads after having taken on partial loads elsewhere. Time and space limitations compel consolidation of loading operations at one or two ports (Tr. 970-71). In short, as the Commission found, it is "not operationally feasible to call at every terminal port" (Com. Rep. 7, R. 1272).

Faced with the offer of an insufficient amount of cargo to justify a call the carrier could be required to serve each port irrespective of whether there is sufficient cargo at the port to justify the call. The inevitable result would be higher rates, satisfactory for Stockton perhaps, but unsatisfactory for the exporter and detrimental to the commerce of the United States. A determination by the ocean carrier to forego the cargo entirely, while of no apparent concern to Stockton, would be equally disadvantageous to the foreign commerce of the United States.

A third alternative is transshipment. There, the shipper delivers the cargo to a port of his selection. If the carrier has declared a receiving dock at that port, it may at its option and its expense have the cargo rehandled and rehailed overland or by barge for

loading at another port (Tr. 761-63). This is far too costly in most cases for the ocean carrier, because it must absorb the full costs of transporting the cargo from the port of delivery to the port of load, and an additional set of terminal charges (Tr. 128-30, 1095-96).⁶ Transshipment is 3-7 times more expensive than equalization (Ex. 53, Tr. 763).

The fourth alternative and the most economical from the carrier point of view is equalization. In general the costs of transportation to the loading port are dependent on the mileage factor. In those cases where direct service to any terminal port in the San Francisco Bay Harbor Complex is impractical or uneconomic, equalization permits the carrier to provide the equivalent of a direct call *at the same cost to the shipper* by absorbing the added increment of inland transportation costs occasioned by the transportation of the cargo to a more distant port where the cargo is loaded. Equalization is thus more economic than a direct call for an unremunerative parcel of cargo. It is always more economic than transshipment (See Com. Rep. 14, R. 1279).

(2) The Shipping Public

Despite Stockton's incredible assertion that no such findings were made (p. 41) the Commission and Examiner did find, fully supported by the record, that service at Stockton is inadequate—not sufficiently regular, frequent or direct for the needs of shippers located adjacent to Stockton (Com. Rep. 8, R. 1273). The shippers so testified (Tr. 812, 844, 908, 982, 1004, 1031).

The PWC presented extensive testimony of shippers located in the areas closest to Stockton.⁷ That testimony demonstrated

6. Under transshipment the terminal charges are paid twice: at the port to which the shipper delivers the cargo and at the loading port. Stockton of course has no objection for that reason to the transshipment mode.

7. Testimony was presented from each of the major commodity groupings moving under equalization: raisins, condensed milk, pencil slats, hides, alfalfa, beginning at Tr. 807, 840, 900, 975, 996, 1023).

that equalization gives "the shipper the best service for his particular need at lowest cost" (I.D. 15, R. 1246). The Commission Report (p. 8, R. 1273) and the Concurring Opinion (p. 10, R. 1315) accepted this testimony.

These advantages may be summarized as follows:

Each of these shippers found it absolutely necessary to have frequent and regular service to meet their shipping needs. They also find it desirable if not mandatory to be able to deliver their cargo to the vessel at or near to the last outbound loading port which, as we have shown, is rarely, if ever, Stockton. These features are vitally important for a number of reasons. For some shippers equalization is a necessity in competing with shippers from other areas to meet the consignee's required delivery dates imposed as the result of consignee's need for strict inventory control or to utilize vessels designated by the consignee (Tr. 811-12, 842-43, 905-6, 999-1001, 1031). Another reason is that delay between delivery to the port and delivery to the consignee adversely affects the out-turn condition of semi-perishable commodities like condensed milk or raisins, or may contribute to deterioration of other items like hides (811-12, 842-43, 980, 999, 1031-33). In many cases shippers require flexibility in ocean services not present at Stockton to enable them to prepare the shipment or to consolidate shipments so that they can meet delivery schedules established by the overseas buyer (Tr. 909, 979-80, 1032).

Transshipment is unsatisfactory because of the extra time it takes and the damage to the cargo caused by rehandling (Tr. 813-14, 845, 984, 1005, 1033).

The shippers unanimously supported equalization since it affords them access to the high level of service obtaining at San Francisco or other ports. Of particular importance to our foreign trade is the effect equalization has upon the ability of these shippers to compete with domestic competitors and those in other countries. Without equalization the shipper must either absorb the costs attendant upon getting his product to the point where

adequate service obtains, or he must forego the foreign sale with a consequent dampening and detrimental effect upon the foreign commerce of the United States, and upon this country's favorable trading balance of payments (Tr. 832-34, 843-45, 855-56, 906-7, 984, 990-91, 994, 998, 1006, 1016, 1021-22, 1034-35, 1138-39).⁸

d. Determinations by Other Federal Agencies

The findings of the Commission respecting tributary areas served via the Golden Gate are expressly consistent with the findings made by the Departments of Commerce and Defense pursuant to Section 8 of the Merchant Marine Act, 1920 (46 U.S.C. § 867) (Com. Rep. 12, R. 1277). That section directs those departments:

" . . . with the object of promoting, encouraging, and developing ports and transportation facilities in connection with water commerce over which it has jurisdiction, *to investigate territorial regions and zones tributary to such ports, taking into consideration the economies of transportation by rail, water, and highway and the natural direction of the flow of commerce*; . . . and to investigate any other matter that may tend to promote and encourage the use by vessels or ports adequate to care for the freight which would naturally pass through such ports."

The Maritime Administration has designated those areas tributary to each San Francisco Bay Harbor Complex port in a series of studies entitled "Port Series", pertinent extracts of which ap-

8. Actually, the record would support conclusions reflecting far wider and more enthusiastic shipper support than the Commission Report indicates. (Compare the Examiner's description, I.D. pp. 16-17, 23; R. 1247-48, 1254; Commissioner Patterson's Concur. Op. 10, R. 1315). Stockton offered no evidence contrary to the shipper testimony summarized above. Indeed, the only witness of a shipper category presented by Stockton was the "sole malcontent shipper" referred to by the Examiner (I.D. 11, R. 1242) whose main objective was not to eliminate equalization, but to obtain greater payments than he was entitled to under the rules.

peared as Exhibits 47-50 in the record. These exhibits are summarized on the map shown on the following page (Figure 1). Each terminal port shown—Sacramento, Stockton, San Francisco, Oakland and Alameda—draws its cargoes from a mutually overlapping tributary area comprising the Northern California hinterland. With specific reference to the contentions of Stockton, the Maritime Administration has determined, taking into account "the economies of transportation and the natural flow and direction of commerce" that the San Joaquin Valley which Stockton claims exclusively for itself is tributary to each of the aforementioned ports.

e. Determinations by the California State Legislature

Throughout the proceeding Stockton reserved its strongest language for a castigation of the notion that Stockton can in any sense be regarded a "Bay Area Port." The Commission (Com. Rep. 12, R. 1277) observed that in 1953 the California State Legislature, following the completion of a comprehensive fact-finding study by the State Senate,⁹ adopted a program of research planning, harbor development and trade promotion for "the San Francisco Bay Area" (Calif. Harbors and Navigation Code, Sec. 1980, et. seq.) defined as:

"... that region served by commercial shipping and transportation passing through the Golden Gate, including tributary trade areas of Central and Northern California."

Stockton in its brief (p. 30) objects to this reference on the basis that such statute and its legislative history are not part of the record. It was wholly proper for the Commission to consider this determination by the California legislature in making its own decisions from *all* the evidence before it. The rules of the Com-

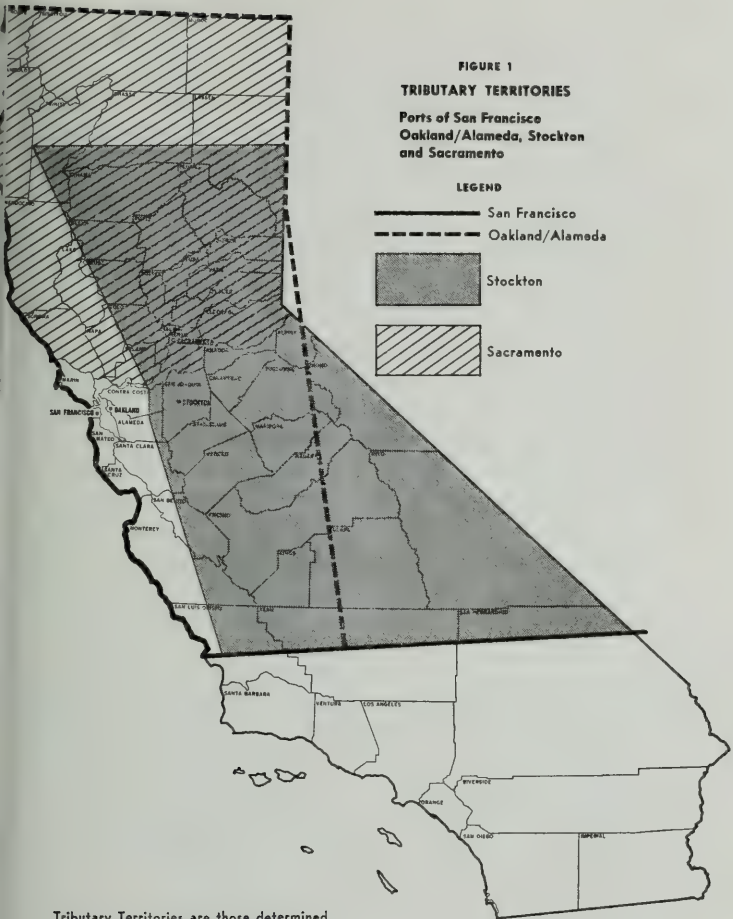
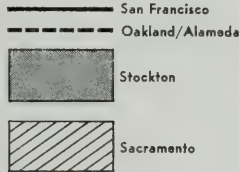
9. *Final Report of the Senate Fact-Finding Committee on San Francisco Bay Ports* (Calif. Legisl. 1951) p. 131, 373, in which the Committee had concluded that the recognition that all ports served through the Golden Gate "comprise *one* harbor is fundamental to progress."

FIGURE 1

TRIBUTARY TERRITORIES

Ports of San Francisco
Oakland/Alameda, Stockton
and Sacramento

LEGEND



Tributary Territories are those determined pursuant to § 8, Merchant Marine Act, 1920, as amended by the Maritime Admin.

Source: Exs. 47-50, inclusive.

mission provide that official notice may be taken of matters as might be judicially noticed by the courts, and also that public documents of the kind here involved may be received in evidence (46 CFR 502.226). That judicial notice may be taken of a state statute and its legislative history is well established. *Keystone Wood Co. v. Susquehanna Boom Co.*, 240 F. 296, 298 (3rd Cir. 1917) *cert. den.* 243 U.S. 655 (1917). (Statute); *Arizona v. California*, 283 U.S. 423, 453 (1930); and *Stasiukovich v. Nicolls*, 168 F.2d 474, 479 (1st Cir. 1948) (Legislative History). In any event Stockton made no attempt or effort to avail itself "upon timely request" of the opportunity provided by the aforementioned Commission rules to show the contrary. Thus assuming *arguendo* that the Commission decision rests upon the California statute, Stockton's remedy was to petition for opportunity to show facts to the contrary at the time it was raised on brief or at the time of the Commission Report in September, 1965. Whatever rights Stockton had in this regard have long since been waived. *Moon v. Celebrezze*, 340 F.2d 926, 929 (7th Cir. 1965); *American President Lines, Ltd.*, 4 FMB 555, 4 Ad.L.2d 820 (1955).

3. STOCKTON'S UNSOUND CONSTRUCTIVE MILEAGE THEORY OF PORT CONTROL

The essential ingredient in Stockton's attack on the findings of the Commission respecting the San Francisco Bay Harbor Complex Ports is a contention that Stockton is exclusively entitled to, and has a legally protected right to, all cargo as to which mileage favors Stockton as compared with mileage to any other port (Com. Rep. 1-4, R. 1279). This contention is based not on substantive facts but first upon pure theory, and secondly, upon a "syllogistic argument" resting on a faulty premise.

Stockton's theory is that mileage (which generally determines the costs of inland transportation) should be the sole determinant in establishing the geographical area tributary to any given ter-

minal port (Stock. Br. 31-37). Stockton uses the current "constructive mileage" table published by California State Public Utilities Commission for motor carrier regulation (Tr. 42-44, 146).¹⁰

The record disclosed several anomalies in this theory which the Commission Report appropriately recognized (pp. 14-15: R. 1279-80 and I.D. 19, R. 1250).

1. Tributary areas so defined continually expand and contract with each new innovation or improvement in highway conditions (Tr. 160-61).

2. Tributary areas are drastically curtailed or expanded, dependent upon the designation of terminal ports. Thus when the PWC, but not the Straits or Indonesian Conferences, named Sacramento a terminal port in 1963, the area purportedly tributary to Stockton for purposes of PWC carriers (but not for other conference carriers) was cut in half, because "that is the way the arithmetic comes out" (Exs. 8, 9; Tr. 64-66).

3. Stockton conceded that some areas westerly of California's eastern border, and in all states easterly thereof, are mutually tributary to all S. F. Bay Harbor Complex Port but presented no rational basis for its inconsistent exclusive claim to the San Joaquin Valley (Tr. 158, 160).

4. The theory produces serious inequities for Stockton's sister ports served through the Golden Gate. The four terminal ports closest to the sea—San Francisco, Oakland, Alameda and Richmond—end up sharing a slender territory along the coast, cunningly designed to prevent their access to the Northern California hinterland. San Francisco ends

10. "Constructive mileage" is road mileage weighted by such factors as traffic lights, bridges, mountainous terrain and other conditions affecting truck traffic (Exs. 4, 8, 9; Tr. 37, 43; Com. Rep. p. 14, R. 1279 fn. 6).

up with a "thin strip" of scenic territory (See Ex. 4). Figure 2 on the following page shows the tributary area claimed by Stockton and also shows the tributary areas allocable to other ports on Stockton's mileage theory.

The Examiner rejected the Stockton inland mileage theory stating (I.D. 19, R. 1250):

"There may be situations where such a method of determining tributary territory would be realistic and appropriate; this is not such a situation."

The Commission agreed, stating (Com. Rep. 14, R. 1279):

"But Stockton's theory is only deceptively simple and does not comport with the principles laid down in prior cases."

Those principles dictated that the geographical relationship of the ports, the "economies of transportation" and "the natural flow of commerce" are all relevant in determining whether the territory surrounding Stockton is "centrally, economically and naturally served" at other Bay Harbor Complex Ports (Com. Rep. 12, 16; R. 1277, 1281).

Beginning at page 31 of its Brief Stockton reiterates a bootstrap argument rejected by both the Examiner and the Commission, based upon a patent misreading of the equalization rule.

Rule 2 of the PWC defines equalization as follows (R. 1264-65):

"Equalization is the absorption by the carrier of the difference between shipper's cost of delivery to ship's tackle at Terminal Dock at nearest conference terminal port and the cost of delivery to ship's tackle at terminal dock and port of equalizing line."

Rule 2(e) as it relates to equalization between California ports, formerly provided:

"... cargo which would normally move from one California terminal port, may be shipped under equalization via another California terminal port."¹¹

11. This language has been eliminated from Rule 2(e) pursuant to the Commission's Amended Order (R. 1304-05). Former Rule 2 is reproduced in its entirety in Appendix B.

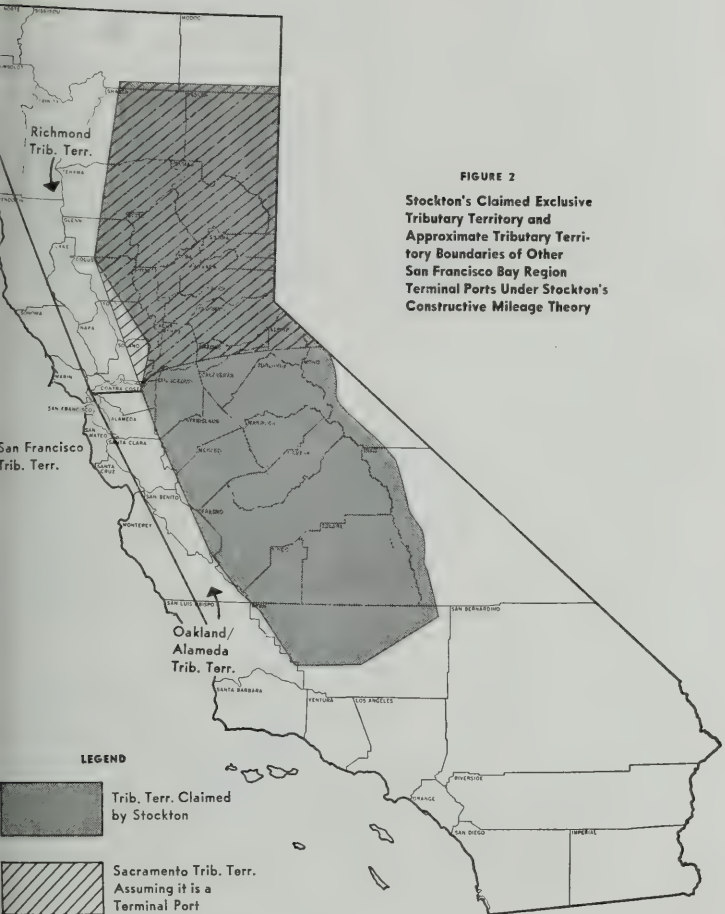


FIGURE 2

Stockton's Claimed Exclusive Tributary Territory and Approximate Tributary Territory Boundaries of Other San Francisco Bay Region Terminal Ports Under Stockton's Constructive Mileage Theory

Source: Stockton and Sacramento as in Ex. 4; Other Ports, Under the Same Assumptions.

Stockton's syllogistic argument (pp. 31-33) is to the effect that the underscored language of Rule 2(e) constitutes proof that cargo equalized on the basis Stockton is the nearest port is tributary only to Stockton.

The former language of the rule was not an acknowledgment or recognition by the Conference that equalized cargo was exclusively tributary to any port. The Conference can't "establish" tributary areas by such means in any event as *all* of the factors considered by the Commission are relevant. Normally in the context of the rule is simply a euphemism for "more cheaply or less cost" (Concur. Op. 9-10, R. 1314-15) since payment of equalization occurs when the shipper requests the same, and when he demonstrates on the basis of cost data furnished to the Conference that his inland transportation costs are cheaper to the terminal port closest to him than to the loading port selected by the carrier (See, Com. Rep. 2, R. 1267).

Possibly in an attempt to bolster the foregoing argument, Stockton objects strenuously to that part of the Commission's order which directed that the "which would normally move" language be removed from the rule (Com. Rep. 23, R. 1288) asserting that equalization can be paid only upon proof of shipper intent to use the nearest port. (Stock. Br. 45).

The Commission disposed of this contention in the following language:

" . . . This apparent restriction has no practical relation to the theory or operation of the rule. Perhaps it was originally intended to make it clear that cargo may be equalized even though it might 'normally' move from another port, thus anticipating any objection on that ground. The rule should be drafted so as to exclude what is clearly not intended as a restriction. . . ." (Com. Rep. 23, R. 1288).

This interpretation is claimed by Stockton to be contrary to the record and erroneous as a matter of law. The testimony of a Conference witness clearly established, however, that whether the shipper had a subjective intent to use the nearest terminal

port if equalization were not paid is not a condition of payment. (See, Tr. 220-221). Neither the definition of the rule, any of the specific conditions of the rule, nor the rule taken as a whole, supports the interpretation that the "would normally move" language is a limitation to its application. Admittedly, the rule could stand clarification and the action of the Commission in ordering the "apparent restriction" to be eliminated was entirely consistent with its obligations under Section 18(b)(1) of the Act (46 U.S.C. § 817(b)(1)) under which carrier tariffs are required to "plainly" show and state, for the benefit of the shipping public, all rules and regulations affecting its rates and charges.

Having shown that the Commission's findings and conclusions respecting the geographical relationships and the tributary area of San Francisco Bay Harbor Complex Ports are fully supported by substantial evidence, we now turn to Stockton's claims that, irrespective of such findings and conclusions, equalization *per se* violates specific provisions of maritime promotional or regulatory statutes.

C. Equalization Is Not Contrary to Section 8, Merchant Marine Act, 1920

Stockton asserts (Stock. Br., Spec. of Error 6, 7; pp. 15-21) that equalization violates *per se* the policy of Section 8 in two respects, (1) that any practice which deprives Stockton of cargo which, under a constructive mileage basis might otherwise move via Stockton, is *a fortiori* a violation of that policy and is unlawful, and (2) that the policy of Section 8 requires all interests, save those of Stockton, to be ignored in determining whether equalization is "contrary to the public interest" in violation of Section 15.

Section 8 charges the Departments of Defense and Commerce (not the Commission) with three duties: (1) to promote, encourage and develop ports, (2) to investigate territorial regions and zones tributary to such ports and (3) to investigate

any matter that may tend to promote and encourage the use by vessels of ports. No power or jurisdiction with respect to Section 8 was vested in the Federal Maritime Commission when the Commission was created by Reorganization Plan No. 7 of 1961 (46 U.S.C. § 1111 (Note) and see, Concur. Op. 1, R. 1306; I.D. 13, R. 1244). Stockton concedes, at page 21 of its brief that Section 8 confers no power to act to promote ports, but asserts most inaccurately that the Commission "ignored" its policy in determining whether equalization is unlawful.

The Commission report is replete with references to the principles and policies of Section 8 (Com. Rep. 10-12, 15-16; R. 1275-77, 1280-81) as is the Initial Decision (I.D. 13-15, R. 1244-46), and even a cursory reading of the same would indicate that though the Commission was not required to do so, consideration was given to such principles and policies.¹²

Section 8 is "indicative of a congressional policy favoring port improvement and development". *Pacific Far East Line v. United States*, 246 F.2d 711, 716 (D.C. Cir. 1957). Section 8 directs the agencies charged with administering it

"to investigate territorial regions and zones tributary to such ports, taking into consideration the economics of transportation by rail, water and highway and the natural direction of the flow of commerce . . .".

This language, as the Commission quite properly recognized (Com. Rep. 12, R. 1277), does not require any mechanical mileage test as a measure of "territorial regions and zones tributary to such ports." If that was the intent Congress would have said so. What is relevant under the statute is the economics of transportation and the natural flow of commerce.

12. Commissioner Patterson felt, and we believe, correctly, that the Commission should not decide the issues with reference to Section 8 in view of the fact that the Commission is not vested with any power or functions by Section 8. (Concur. Op. 4, R. 1309)

This view is consistent with an earlier restatement of the policy of Section 8 in which the Commission's predecessor¹³ had said:

"That section requires, all other factors *being substantially equal*, that a *given geographical area* and its ports shall receive the benefits of or be subject to the burdens naturally or incident to its proximity or lack of proximity to another *geographical area*. To the extent, therefore, that the ports of a *given geographical area* give or can give adequate transportation services, we look with disfavor on equalization rules which divert traffic away from the natural direction of the flow of traffic." (emphasis supplied) (*City of Portland v. Pacific Westbound Conference*, *supra* 4 F.M.B. at 679).

In the *City of Portland* case the Commission's predecessor had focused its concern, not upon individual ports, but upon "a given geographical area and its ports." The Commission here explained its rejection of the physical separation of Stockton from San Francisco Bay (or the mileage factor) as the sole determinant in invoking the protective policy of Section 8:

"The delineation of a 'given geographical area' will almost always of necessity involve the inclusion of ports whose location from specified inland points will vary in distance or mileage. Thus, mileage alone is not the determinative factor." (Com. Rep. 12, R. 1277).

It is ironic that Stockton on the one hand, at page 21 of its opening brief, charges the Commission with ignoring the policy of Section 8, yet later at page 35, with equal vigor, castigates the Commission for relying upon a report implementing that statute prepared by the government agencies charged with administration of that Section. We have seen that the Departments of Commerce and Defense in the exercise of their functions under Section 8

13. This was before the Reorganization Plan of 1961, *supra* and at a time when the Agency then speaking (unlike the FMC) did have some responsibility under Section 8.

have determined that Stockton's tributary area is equally tributary to other S. F. Bay Harbor Complex Ports. In so doing they implicitly rejected the mechanical mileage test which Stockton claims Section 8 requires. For the Commission now to do likewise lends affirmative support to the conclusion that the Commission's focus upon geographical areas, rather than upon individual competing ports, is entirely consistent with any policy envisioned by Section 8.¹⁴

D. Equalization Is in the Public Interest

Stockton, at the outset, had claimed that equalization operated "to the detriment of the commerce of the United States," and was "contrary to the public interest," in violation of Section 15 of the Shipping Act, 1916.

The Commission, having weighed the various interests which, in the aggregate, comprise the public interest, found that not only was equalization not contrary to the public interest, but affirmatively concluded that equalization:

"reflects an overall economic good, tangible benefit to the public at large, and an important transportation justification" (Com. Rep. 20, R. 1285).

It appears to be Stockton's belief that the "public interest" is somehow identical with Stockton's self-interest, a myopic viewpoint which is said to be required by the policy of Section 8. (Stock. Br. 19-21). The various interests—the shippers, ocean carriers, and ports must each be considered:

14. Nor does the fact that Stockton was developed with the assistance of public, including federal funds, establish any prior right under Section 8, as Stockton contends (Stock. Br. 18). This is answered convincingly by Commissioner Patterson who pointed out that the investment of federal funds "depends upon commercial potentialities, not on future rights. Once made, the investment does not thereafter create legal rights to a flow of business or entitle anyone to anything, but only creates opportunities to exploit." (Concur. Op. 16-17, R. 1321-22).

1. THE SHIPPER

The benefits to shippers resulting from equalization have been recapitulated at pages 23-25, *supra*. Perhaps the most accurate summary of the advantages to shippers appears in the Examiner's Initial Decision (p. 16, R. 1247):

"Equalization is of substantial advantage to shippers. San Francisco provides many more direct sailings, on a regular basis, than does Stockton; it has a better climate, which is of importance in the case of certain perishable cargoes; and there is no delay in getting cargo aboard a vessel departing for the desired destination. San Francisco has a wider range of facilities to handle various types of cargo. . . . The faster service which shippers are thus able to give their foreign buyers through San Francisco, while keeping their costs down through equalization, is of benefit to the commerce of the United States and the public interest."

2. THE OCEAN CARRIER

The benefits which equalization affords to shippers are mutual benefits with those received by the ocean carrier. They have been described at pages 21-23, *supra*. They include:

"[The] benefit (of) not having to make the extra 75-nautical-mile journey to Stockton for amounts of cargo insufficient to support regular berth service." [Concur. Op. 10, R. 1315].

The carrier by concentrating loading operations at the principal loading port of lesser cost thus avoids the need to call at other ports for unremunerative cargo which "gives the vessel latitude in loading and scheduling and the flexibility to avoid uneconomical calls" (Com. Rep. 7, R. 1272).

3. THE PORTS

Even if it can be assumed that cargo presently equalized on the basis Stockton is the nearest port which would otherwise move through Stockton—port revenues are not lost. The same charges

and the same revenues which Stockton allegedly "loses" through equalization flow to San Francisco or other loading port (Tr. 133).¹⁵ If equalization is terminated, the Port of San Francisco is damaged (Tr. 1134-35). San Francisco, unlike Stockton is wholly financed out of revenues, and it is necessary for the port to meet its projected revenues to service its bonded indebtedness (Tr. 1143-45). Clearly Stockton made no better a case than San Francisco for protective treatment in this regard.

4. THE ALLEGED DISADVANTAGES TO STOCKTON

The short answer to Stockton's contentions that equalization deprives it of cargo or revenues resulting therefrom (p. 19) is that Stockton is not fundamentally entitled to the cargo which is equalized on the basis it is the nearest port to the shipper. (Com. Rep. 14, R. 1279; Concur. Op. 16, R. 1321), and it is no more entitled to the revenue produced by such cargo than it is to the cargo itself. Moreover, as the Commission found, Stockton's claimed "lost revenue" figures were "not valid" because Stockton would have had additional labor costs to produce such revenue and

"as Stockton argues elsewhere, not all the equalized cargo would have gone to Stockton but for equalization, and the number of additional vessels which would have gone to Stockton is highly speculative" (Com. Rep. 14, R.1279; Tr. 131-33, 198-99; Ex. 16).

Stockton's phenomenal growth, despite the supposed detriment of equalization is fully documented on the record (Com. Rep., 22, R.1287). The Commission observed:

"Moreover, it should be noted that even with equalization, Stockton's growth since 1957 has put it ahead of the ports of San Francisco, Oakland and Alameda combined, in export

15. The Conference equalization rule permits equalization between any of the San Francisco Bay Harbor Complex ports. Accordingly each such port receives benefit and detriment from the rule in varying degrees.

tonnage. . . . Thus, equalization has not seriously affected Stockton's competitive position." (See also, Tr. 144, 1146-47; Exs. 44-46).

Stockton's concern (Stock. Br. 19) for carriers which serve Stockton is almost wholly a fabrication. The carriers serving Stockton are, of course, the same carrier respondents in the proceeding who, with one exception,¹⁶ enthusiastically endorse and utilize equalization. (Com. Rep. 5-6, R.1270-71). Even to the extent carriers serving Stockton are "deprived" of cargo as the result of equalization, no contrariety to the public interest is shown because, as Commissioner Patterson notes (Concur. Op. 13, R. 1318):

" . . . equally carriers serving San Francisco would be deprived of cargo under any other arrangement, and Stockton has not established any superior right to offset the conveniences of the shipping public and carriers."

5. THE INTERESTS IN THE AGGREGATE

We submit the Commission correctly considered each of these interests and it was entirely in accord with the public interest language of Section 15 for it to do so. Section 15 is a self-contained regulatory measure. *Alcoa Steamship Company v. Federal Maritime Commission*, 321 F.2d 756, 761 (D.C. Cir. 1963). Again, this is a matter for determination based on substantial evidence. It can

16. Pacific Far East Line (PFEL) endorsed equalization in general, but criticized it as it applied to Stockton because of the peculiar relationship it has with that port. It called 45 times at Stockton in 1963, but only 17 of such vessels loaded any general cargo. The Commission observed that:

"Respondent PFEL, the only carrier that was critical of equalization against Stockton frankly considers its position to be 'more advantageous than others insofar as calling at the Port of Stockton. . . . we have contracts for bulk cargoes for justification to put us up to the Port of Stockton which other lines do not have.' Thus PFEL feels it could get 'the lion's share' of any additional tonnage going through Stockton. Still PFEL now transships cargo from Stockton by truck and also equalizes against Stockton." (Com. Rep. 21, R. 1286, fn. 9; see, Tr. 496, 526-7).

not be argued, on the basis of the vague policy of Section 8 of the Merchant Marine Act, 1920, or otherwise, that Congress had intended the Commission to ignore all interests, excluding those of Stockton in administering the Shipping Act, 1916.

The Commission acted in accordance with sound administrative discretion when it concluded (p. 20, R. 1285):

"But the public interest is much larger than the needs or desires in the Stockton area. The equalization under consideration here reflects an overall economic good, tangible benefit to the public at large, and an important transportation justification."

E. No Discrimination Between Ports in Violation of Sections 15 and 16 (First)

The Commission concluded that whatever prejudice or discrimination Stockton suffers it is not undue, unjust or unreasonable within the meaning of Sections 15 and 16 (First) of the Shipping Act (Com. Rep. 13-14, R. 1278-79).

The bare legal argument of Stockton begins from an extreme position. If cargo would move through Stockton if it were not for equalization, then says Stockton equalization is *ipso facto* unjustly discriminatory or unduly prejudicial to Stockton, because of the alleged "diversion" of cargo (Stock. Br., Spec. of Error 7, p. 25). This argument, however, overlooks the essential predicate upon which any assertion of diversion or deprivation of cargo must be based. That is, that Stockton must establish some prior and superior right to cargo which, but for equalization, would move via Stockton. Such right must be shown to be superior to that of Stockton's sister ports in the San Francisco Bay Harbor Complex and to the interests of shippers and carriers serving those ports. The Commission's factual findings precludes the existence of such a right.

One key to the Commission's decision rejecting Stockton's claims of unjust discrimination and undue prejudice in violation of Sec-

tions 15 and 16(First) is its findings and conclusions that cargo claimed to be exclusively tributary to Stockton is also tributary to San Francisco and other Bay Harbor Complex Ports. (Com. Rep. 13-14, R. 1278-79). Whatever discrimination or prejudice Stockton suffers from the purported diversion of cargo, is not "unjust" or "undue" because its right to the cargo is not exclusive or superior to the rights of the other ports.

The other key to the Commission ruling is its finding that there is "ample economic and cost justification for the discrimination such as it is" (Com. Rep. 14, R. 1279). At page 11 (R. 1316) of his concurring opinion, Commissioner Patterson finds this balancing of interests of paramount importance in determining whether any disadvantage suffered by Stockton is contrary to law:

"Undue, unjust, or unreasonable discrimination, prejudice, and preference involve choices creating inequality of treatment of similarly situated persons for no reason. There are legitimate economic reasons for the carrier's rule based on the different situations at the two ports. (After referring to the advantages to carriers and shippers, Com. Patterson continued) . . . the rights of Stockton to be used as a port do not transcend these mutual advantages. . . ."

The Commission's determination under Sections 15 and 16(First) that Stockton is not subjected to undue, unreasonable or unjust discrimination must be sustained if supported by substantial evidence. The question of what is contrary to the standards of Sections 15 and 16(First) or unjustly discriminatory or unfair:

". . . obviously turns upon a determination of facts—a function committed by Congress to the Commission, an expert body whose findings in this regard are not lightly to be disregarded by a reviewing court." *Alcoa Steamship Company v. Federal Maritime Com.*, 321 F.2d 756, 759 (D.C. Cir. 1963). See also *Swayne & Hoyt v. United States*, 300 U.S. 297 (1937).

F. The Commission's Decision Is Consistent with Prior Decisions

Stockton's argument (Stock. Br. 38-45) that the Commission's Report is inconsistent with prior decisions contains a fundamental misconception as to the role of a court reviewing an administrative order. It is not the role of this Court to determine whether each administrative decision is consistent with prior cases of the same agency, but rather whether the decision under review is in accord with the law and is supported by the record. *F.C.C. v. WOKO, Inc.*, 329 U.S. 223 (1946); *Wm. N. Feinstein & Co. v. United States*, 317 F.2d 509, 512 (2nd Cir. 1963) where the court said:

"Second, plaintiff contends that the decision of the Commission should be set aside as arbitrary and capricious because of its alleged inconsistency with the Commission's earlier decision. . . . This contention is not sustainable; the mere fact of inconsistency with a prior decision, even assuming such inconsistency had been demonstrated, is not a valid basis for setting aside the later decision of an administrative agency. . . . In proceedings of this kind, a court reviews no more than the particular administrative order which the plaintiff has challenged and seeks to determine only whether the record in the case before it contains substantial evidence to support the findings upon which the order is based. . . . Because the record in a given prior proceeding is not before the court, any comparison of the kind which plaintiff seeks to have us make between an earlier and a later agency decision is neither possible or appropriate." 317 F.2d at 512.

The ability of the Commission to adapt to changed ideas, its experience, and new circumstances is one of the strengths of the administrative process. *Shawmut Assoc. v. S.E.C.*, 146 F.2d 791, 796 (1st Cir. 1945). Thus, the extent to which the Commission is fashioning new standards for testing equalization based upon a balancing of interests does not constitute any ground for judicial review.

Further, any contention that the Commission's decision is inconsistent with prior cases is ludicrous in view of the painstaking care which the Commission and the Examiner took to reconcile their respective decisions with the prior cases (See, Com. Rep. 11-16, R. 1276-81; I.D. 13-19, R. 1244-50).

Those prior cases had established that Equalization is not unlawful in principle. *Beaumont Port Commission v. Seatrain Lines, Inc.*, 2 USMC 500, 504 (1941); *City of Mobile v. Baltimore Insular Line*, 2 USMC 474, 486 (1941).

In every case in which the Commission or its predecessors have outlawed or modified an equalization or equivalent practice, they have done so on the basis that the practical consequence of equalization or absorption was to draw cargo away from the tributary area served by a group of ports to another group of ports serving a geographically distinct tributary area. (See, *City of Portland v. Pacific Westbound Conference*, *supra*).

In the *City of Portland* case, it was of crucial significance that equalization had the effect of drawing cargo from the area tributary to the Northwest Ports (Portland, Seattle, etc.) to the ports of California serving an entirely distinct tributary area. The Board stated:

"To the extent, therefore, that ports of a given geographical area give or can give adequate transportation services, we look with disfavor on equalization rules or practices which divert traffic away from the natural direction of the flow of traffic." (4 FMB at 679.)

The Commission found a parallel to equalization within the Bay Harbor Complex in the case of *Port Commission of Beaumont v. Seatrain Lines*, 2 USMC 699 (1943). In that case, the so-called second *Beaumont* case, the U.S. Maritime Commission (a predecessor agency) permitted a carrier to equalize on cargo loaded at Texas City with respect to cargo originating in areas adjacent to

Houston and Galveston, Texas, but not cargo originating adjacent to Beaumont, Texas. The geographical relationship of Texas City, Houston and Galveston is comparable to that of San Francisco, Stockton and other Bay Area ports, respectively.¹⁷

Stockton, throughout the proceeding and now, attempted to distinguish the second *Beaumont* case on the basis of supposedly "unique" facts (Stock. Br. 42-43). It is contended that Houston does not occupy a position corresponding to Stockton, but both are located on inland waterways connecting with a bay on which other ports are situated. Stockton further claims a factual difference because, in the *Beaumont* case, the carrier economics favoring equalization centered around the cost of erecting special facilities at a port, rather than, as here, the costs incurred in moving from one port to another. This distinction is not material.

Additional precedent for the Commission's decision in the instant case may be found in the *City of Portland* case where the Commission made it clear that equalization is justifiable on grounds that service at the port area "losing" the cargo is not adequate for the needs of shippers there (4 FMB at 679 quoted at p. 43, *supra*). As we have seen, Stockton affords inadequate service for local shippers of general cargo to Far East ports.

The same precedents explain why the Commission ordered terminated equalization on cargo originating in areas tributary to the San Francisco Bay Harbor Complex Ports and loaded at Los Angeles/Long Beach. The Commission found that Los Angeles/Long Beach serve a different tributary area and no benefits to shippers or carriers as justification for equalization in that situation (Com. Rep. 26, R. 1291).

17. The Commission quite obviously chose its language in the instant report with care in view of the geographical parallel with the second *Beaumont* case. In that case (as in this case) it noted—the "geographical relationship of the ports," the "peculiar characteristics" of the carrier's operation—the location of "Texas City and Galveston on Galveston Bay" which is also the approach to Houston, concluding ". . . the three ports may be described as Galveston Bay Ports." (2 USMC 699 at 701, 702).

G. There Is No Violation of Section 205 of the Merchant Marine Act, 1936

Stockton contends (Stock. Br. 22-23), without extensively arguing the point, that the equalization is *per se* a violation of Section 205 of the Merchant Marine Act, 1936.

Here, as in the case of Section 8 of the Merchant Marine Act, 1920, no function under Section 205 was transferred to the Commission under Reorganization Plan No. 7 of 1961. While not required to do so, the Commission has nonetheless given full consideration to the policy expressed in Section 205. (Com. Rep. 22-23, R. 1287-88).

The policy of Section 205 requires, at most, that carriers, or conferences of carriers, may not prevent other carriers from serving a federally assisted port by establishing different ocean rates than that established at an adjacent port.¹⁸

The Commission determined this policy was not violated, stating:

"The rules, as applied, permit equalization in favor of Stockton to exactly the same extent as against it. Respondents comply literally with the statute by serving Stockton at the same rates which they charge at the nearest port regularly served by them, since the rates are the same for all bay area terminal ports. If equalization is considered to change the base rates from any such port respondents are in compliance with the statute because they offer the same equalization to shippers who wish to load at Stockton (Com. Rep. 23, R. 1288).

Stockton attempts to twist Section 205 into a policy disfavoring any competitive practice which prevents or discourages service

18. Section 205 states:

"... it shall be unlawful for any common carrier by water either directly or indirectly . . . to prevent or attempt to prevent any other such carrier from serving any port (serving ocean-going vessels and improved with federal funds) at the same rates which it charges at the nearest port already regularly served by it."

at Stockton. The assertion throughout Stockton's Brief (pp. 2, Spec. No. 10, 13, pp. 22-23) that the equalization rule "prevents" carriers from serving Stockton which would otherwise send their vessels to Stockton is not supported by the record.¹⁹

Except for the intermittent offerings of bulk or bottom cargo there is insufficient cargo at Stockton to justify calls there. The carrier witnesses testified unequivocally that direct service would not increase if equalization ceased due to operational problems and the fact that there would be insufficient cargo offerings. (Tr. 527, 881-2, 969-70, 1063-64, 1085).²⁰ The Commission accepted this uncontradicted testimony stating that the number of additional calls at Stockton in the event of termination of equalization is "highly speculative." (Com. Rep. 14, R. 1279).

As the Commission Report (p. 21, R. 1286) and the Concurring Opinion (p. 13, R. 1318) stated, equalization enables all conference carriers to be able to compete with each other with a minimum of economic waste, at every terminal port in the San Francisco Bay Harbor complex while still providing ocean service at the same rate at every terminal port.

Section 205 does not, nor was it designed to prevent competition between carriers, nor was it intended, as Stockton would have it, to force carriers to go to Stockton on an uneconomic basis. In any event equalization is in compliance with Section 205.

We repeat, however, this is an academic analysis so far as this case is concerned because it is the Commission's order that

19. The quote on p. 22 of Stockton's Brief from the Commission's Report to the effect that Carriers find that competition "compels them to equalize" is part of the recital of charges made against equalization by those said to be opposed to the rule.

20. Even the one line, PFEL, that criticized equalization believed that initially there would be an increase in direct calls by its competitors, but that shortly thereafter it would be apparent that it would be economically attractive to PFEL only because of its bulk cargo commitments, and not to the others (Tr. 527). As pointed out previously the Carriers would avoid direct calls at Stockton by use of the economically wasteful use of transshipment.

is under review and the Commission has no responsibility or authority to issue an order under Sec. 205.

H. Equalization Does Not Violate Section 16(Second) of the Shipping Act, 1916.

Section 16(Second) makes it a criminal offense

"to allow any person to obtain transportation at less than the regular rates or charges then established and enforced on the line of such carrier by means of false billing, false classification, false weighing, false report of weight, or by any other unjust or unfair device or means."

We find it mystifying, if not improper, for Stockton to charge a violation of Section 16(Second) when it made no such contention before the Examiner or the Commission. This provision, added to the Act in 1936, was designed to protect carriers from the coercion of large and overbearing shippers [H. Rept. No. 2598, 74 Cong., 2d Sess., p. 2]. The Commission and its predecessors and the courts have long interpreted as an "unjust or unfair device or means" under this provision, procedures designed to produce active concealment of reduced rates. The conduct made criminal by Section 16(Second) is a disequality of treatment accompanied by an act of concealment. *United States v. Peninsular and Occidental SS Co.*, 208 F.Supp. 957 (SDNY 1962).

The Commission has dealt with and properly disposed of all contentions of Stockton which could conceivably result in a finding that Section 16(Second) has been violated.²¹

Stockton now claims, however, where equalization is paid to a shipper who theoretically might have been willing to pay the

21. Stockton claimed equalization violated Section 18(b)(1) of the Shipping Act, 1916, in that it creates inequalities and is unduly and unreasonably preferential as between shippers, and that it "serves as a cloak for malpractices," i.e. rebating. The Commission rejected each claim after correcting a tariff application not pertinent here. (Com. Rep. 17-21, 23-25; R. 1282-86, 1288-90). Stockton has not objected to the Commission's findings and conclusions in this regard.

higher costs of shipping the cargo to a more distant loading port if there were no equalization that an "unnecessary gratuitous rebate" has been paid, in violation of Section 16(Second).²² When this case was before the Examiner and the Commission, this same theoretical circumstance was claimed by Stockton to be a "dissipation of carrier revenues" and detrimental to commerce and contrary to the public interest in violation of Section 15. The Commission rejected this claim (Com. Rep. 21-23, R. 1286-88) and Stockton does not challenge that conclusion.

Stockton's contention that equalization is administered in violation of Section 16(Second) depends upon a tortured construction of the Conference equalization rule. The former language of PWC tariff Rule 2(e) has been discussed heretofore, p. 32, *supra*. It provided, in effect, that cargo "which would normally move" from one California terminal port may be shipped under equalization via another such port. It is asserted (Stock. Br. 24-25), that this language requires proof of the subjective intent of the shipper—i.e., that in the absence of equalization he would use the nearest port. As we have seen, pages 32-33, *supra*, the rule was never intended to be nor has it been interpreted in that fashion, and the Commission agreed (Com. Rep. 23, R. 1288). There can thus be no claim that there is any departure from the tariff rules in violation of Section 16 (Second), and the amendment of the tariff rule to eliminate the "which would normally move" language in accordance with the Commission's Order removes any lingering doubt on that score.

22 At page 24 of its Brief, Stockton attempts to make capital (of the language of the Commission's Report (p. 8)) that "If there were no equalization many perishable commodities would still move through San Francisco rather than Stockton." It is not clear whether the Commission is speaking of cargo which is presently equalized. If equalization were eliminated shippers presently equalizing would either have to absorb the costs of shipping via a distant port with adequate service, utilize the nearest port irrespective of whether service is adequate, or forego the export sale. (pp. 24-25, *supra*)

The Examiner pointed out, and the Commission and Commissioner Patterson agreed (Com. Rep. 21-22; Concur. Op. 13, R. 1286-87, 1318) that while some Stockton area shippers might possibly ship via San Francisco even if there were no equalization:

"... there is no practicable way to determine how a shipper would act in any instance if equalization were not paid, and even if there were it would be clearly discriminatory to allow equalization only to shippers whose business could not otherwise be obtained. To find this argument of complainant's controlling, it would be necessary to attribute surprisingly bad judgment to respondents and complainant, the former for offering equalization at all and the latter for bothering to prosecute this proceeding." (I.D. 25-26, R. 1257)

I. No Violation of the Fifth Amendment

Stockton claims offhandedly that its arguments, heretofore answered in this brief, establish a deprivation of property without due process of law in violation of the Fifth Amendment to the Constitution (Stock. Br. 48).

We have shown that the cargo which Stockton claims to have been "diverted" from it is not the "property" of Stockton and that it has no legally protected right to have it move over its facilities. We have also shown that the Commission Report and Order is warranted by law and supported by substantial evidence.

In these circumstances there can be no violation of the Fifth Amendment.

IV.

CONCLUSION

The administrative agency hearings in this matter were extensive and thorough. Following the hearing, the Presiding Examiner wrote a thoughtful and orderly Initial Decision of some 32 pages in length, which made complete findings of the background facts, and after full analysis of the law reached his conclusion, rejecting

Stockton's claims. One year later, after the matter had again been fully briefed and argued, the Commission issued its Report and Order of 27½ pages, adopting the Examiner's Initial Decision, again fully supported by findings and conclusions as required by the APA. A comprehensive Concurring Opinion of some 26 pages supplements the Commission Report, reinforcing the reasons why Stockton's claim must be rejected.

In its efforts to terminate equalization and to promote its self-interest contrary to the interests of other ports, shippers and carriers and the public interest generally, Stockton raised before the Examiner and Commission every conceivable objection to the Conference equalization rules. The Examiner and Commission having rejected these claims, Stockton resumes and extends the same claims in this action for judicial review.

Stockton here charges certain findings and conclusions by the Commission are unwarranted by law and unsupported by substantial evidence. It has the burden of making a clear and convincing showing of such alleged errors. With the agreement of both levels of the Administrative agency, both possessing expertise and special qualifications in the maritime regulatory field, Stockton's burden is an extremely heavy one. We submit it has completely failed in discharging that heavy burden.

Stockton has not really attempted to show the findings and conclusions of the Commission which it challenges are unwarranted by law and unsupported by substantial evidence. Instead it has merely renewed contentions made before the Agency, inviting this court to substitute its judgment on matters which are confided by statute to the Agency expert in its field and which were determined by the Agency entirely consistent with the statutes it is directed to administer.

In the foregoing discussion in this Brief we have, on the other hand, attempted to show affirmatively that the Commission Report is clearly warranted by law and abundantly supported by substan-

tial evidence and within its authorized discretion and statutory responsibility. This Court, on judicial review, is not required, nor indeed permitted, to substitute its judgment for that of the Agency as to findings drawn from such evidence.

Respectfully submitted,

EDWARD D. RANSOM
GORDON L. POOLE
LILICK, GEARY, WHEAT, ADAMS
& CHARLES

311 California Street
San Francisco, California 94104

*Attorneys for Intervenors Pacific
Westbound Conference and
Its Member Lines*

Dated: August 11, 1966.

Certificate of Counsel and of Service

I certify that, in connection with the preparation of this brief, I have examined Rules 18 and 19 of the United States Court of Appeals for the Ninth Circuit, and that, in my opinion, the foregoing brief is in full compliance with those rules.

I further certify that I have this day served the foregoing document upon all parties of record in this proceeding by mailing, by air mail, postage prepaid, one copy to Walter H. Mayo III and Irwin A. Seibel, attorneys for the respondents, and by mailing three copies thereof, by regular first-class mail, postage prepaid, to Albert T. Cronin, Jr. and J. Richard Townsend, attorneys for the petitioner, and one copy thereof to Leonard G. James, attorney for intervenors Pacific Straits Conference and Pacific/Indonesian Conference and member lines, and Miss Miriam E. Wolff, attorney for intervenor San Francisco Port Authority.

Dated at San Francisco, California, August 11, 1966.

GORDON L. POOLE

*Attorney for Intervenors
Pacific Westbound Conference
and Its Member Lines*

(Appendices Follow)



Appendix A

STATUTES AND REGULATION RELIED UPON

1.

Section 15 of Shipping Act, 1916 (46 U.S. Code 814)

"That every common carrier by water, or other person subject to this Act, shall file immediately with the Commission a true copy, or, if oral, a true and complete memorandum, of every agreement with another such carrier or other person subject to this Act, or modification or cancellation thereof, to which it may be a party or conform in whole or in part, fixing or regulating transportation rates or fares; giving or receiving special rates, accommodations, or other special privileges or advantages; controlling, regulating, preventing, or destroying competition; pooling or apportioning earnings, losses, or traffic; allotting ports or restricting or otherwise regulating the number and character of sailings between ports; limiting or regulating in any way the volume or character of freight or passenger traffic to be carried; or in any manner providing for an exclusive, preferential, or cooperative working arrangement. The term 'agreement' in this section includes understandings, conferences, and other arrangements.

The Commission shall by order, after notice and hearing, disapprove, cancel or modify any agreement, or any modification or cancellation thereof, whether or not previously approved by it, that it finds to be unjustly discriminatory or unfair as between carriers, shippers, exporters, importers, or ports, or between exporters from the United States and their foreign competitors, or to operate to the detriment of the commerce of the United States, or to be contrary to the public interest, or to be in violation of this Act, and shall approve all other agreements, modifications, or cancellations. * * *

2.

**Section 16 (First) and (Second) of Shipping Act, 1916
(46 U.S. Code 815)**

** * * * *

That it shall be unlawful for any common carrier by water, or other person subject to this Act, either alone or in conjunction with any other person, directly or indirectly:

First. To make or give any undue or unreasonable preference or advantage to any particular person, locality, or description of traffic in any respect whatsoever, or to subject any particular person, locality, or description of traffic to any undue or unreasonable prejudice or disadvantage in any respect whatsoever: * * *.

Second. To allow any person to obtain transportation for property at less than the regular rates or charges then established and enforced on the line of such carrier by means of false billing, false classification, false weighing, false report of weight, or by any other unjust or unfair device or means.

* * * * *

3.

Section 18(b)(1) of Shipping Act, 1916 (46 U.S. Code 817(b)(1))

"From and after ninety days following October 3, 1961 every common carrier by water in foreign commerce and every conference of such carriers shall file with the Commission and keep open to public inspection tariffs showing all the rates and charges of such carrier or conference of carriers for transportation to and from United States ports and foreign ports between all points on its own route and on any through route which has been established. Such tariffs shall plainly show the places between which freight will be carried, and shall contain the classification of freight in force, and shall also state separately such terminal or other charge, privilege, or facility under the control of the carrier or conference of carriers which is granted or allowed, and any rules or regulations which in anywise change, affect, or determine any part or the

aggregate of such aforesaid rates, or charges, and shall include specimens of any bill of lading, contract of affreightment, or other document evidencing the transportation agreement. Copies of such tariffs shall be made available to any person and a reasonable charge may be made therefor. The requirements of this section shall not be applicable to cargo loaded and carried in bulk without mark or count, or to cargo which is softwood lumber. As used in this paragraph, the term "softwood lumber" means softwood lumber not further manufactured than passing lengthwise through a standard planing machine and crosscut to length, logs, poles, piling, and ties, including such articles preservatively treated, or bored, or framed, but not including plywood or finished articles knocked down or set up."

4.

Section 8 of Merchant Marine Act, 1920 (46 U.S. Code 867)

"That it shall be the duty of the board, in cooperation with the Secretary of War, with the object of promoting, encouraging, and developing ports and transportation facilities in connection with water commerce over which it has jurisdiction, to investigate territorial regions and zones tributary to such ports, taking into consideration the economies of transportation by rail, water, and highway and the natural direction of the flow of commerce; to investigate the causes of the congestion of commerce at ports and the remedies applicable thereto; to investigate the subject of water terminals, including the necessary docks, warehouses, apparatus, equipment, and appliances in connection therewith, with a view to devising and suggesting the types most appropriate for different locations and for the most expeditious and economical transfer or interchange of passengers or property between carriers by water and carriers by rail; to advise with communities regarding the appropriate location and plan of construction of wharves, piers, and water terminals; to investigate the practicability and advantages of harbor, river, and port improvements in connection

with foreign and coastwise trade; and to investigate any other matter that may tend to promote and encourage the use by vessels of ports adequate to care for the freight which would naturally pass through such ports: *Provided*, That if after such investigation the board shall be of the opinion that rates, charges, rules, or regulations of common carriers by rail subject to the jurisdiction of the Interstate Commerce Commission are detrimental to the declared object of this section, or that new rates, charges, rules, or regulations, new or additional port terminal facilities, or affirmative action on the part of such common carriers by rail is necessary to promote the objects of this section, the board may submit its findings to the Interstate Commerce Commission for such action as such commission may consider proper under existing law."

5.

Section 205 of Merchant Marine Act, 1936 (46 U.S. Code 1115)

"Without limiting the power and authority otherwise vested in the Commission, it shall be unlawful for any common carrier by water, either directly or indirectly, through the medium of an agreement, conference, association, understanding, or otherwise, to prevent or attempt to prevent any other such carrier from serving any port designed for the accommodation of ocean-going vessels located on any improvement project authorized by the Congress or through it by any other agency of the Federal Government, lying within the continental limits of the United States, at the same rates which it charges at the nearest port already regularly served by it."

6.

**Section 10(e) of Administrative Procedure Act
(5 U.S. Code 1009(e))**

"SCOPE OF REVIEW.—So far as necessary to decision and where presented the reviewing court shall decide all relevant questions of law, interpret constitutional and statutory provisions,

and determine the meaning or applicability of the terms of any agency action. It shall (A) compel agency action unlawfully withheld or unreasonably delayed; and (B) hold unlawful and set aside agency action, findings, and conclusions found to be (1) arbitrary, capricious, an abuse of discretion, or otherwise not in accordance with law; (2) contrary to constitutional right, power, privilege or immunity; (3) in excess of statutory jurisdiction, authority, or limitations, or short of statutory right; (4) without observance of procedure required by law; (5) unsupported by substantial evidence in any case subject to the requirements of sections 7 and 8 or otherwise reviewed on the record of an agency hearing provided by statute; or (6) unwarranted by the facts to the extent that the facts are subject to trial de novo by the reviewing court. In making the foregoing determinations the court shall review the whole record or such portions thereof as may be cited by any party, and due account shall be taken of the rule of prejudicial error."

7.

Fifth Amendment to Constitution of the United States

"No person shall * * * be deprived of life, liberty, or property, without due process of law; nor shall private property be taken for public use, without just compensation."

8.

46 CFR 502.226 (Rule 13(f) of the Rules of Practice and Procedure, Federal Maritime Commission)

"(a) Official notice may be taken of such matters as might be judicially noticed by the courts, or of technical or scientific facts within the general knowledge of the Commission as an expert body: *Provided*, That where a decision or part thereof rests on the official notice of a material fact not appearing in the evidence in the record, the fact of official notice shall be so

stated in the decision, and any party, upon timely request, shall be afforded an opportunity to show the contrary.

(b) Whenever there is offered in evidence (in whole or in part) a public document, such as an official report, decision, opinion, or published scientific or economic statistical data issued by any of the executive departments (or their subdivisions), legislative agencies or committees, or administrative agencies of the Federal Government (including Government-owned corporations), or a similar document issued by a state or its agencies, and such document (or part thereof) has been shown by the offeror to be reasonably available to the public, such document need not be produced or marked for identification, but may be offered in evidence as a public document by specifying the document or relevant part thereof."

Appendix B**RULE NO. 2 OF PACIFIC WESTBOUND CONFERENCE**

*(As set forth in Appendix A of Report of Federal
Maritime Commission in Docket No. 1086)*

(The "Equalization rule", so far as it relates particularly to the Port of Stockton, is underlined.)

Subject to Rules 5, 7 & 9, rates are based on direct loading at Conference terminal loading ports or docks. However, individual member lines may, in lieu of a direct call, absorb the cost of transshipment between terminal ports; or between terminal ports and non-terminal ports; also between non-terminal ports. Reference to non-terminal port absorption applies only if the non-terminal ports have the required minimum tonnage as specified in Rule No. 9, or elsewhere in this tariff. Carriers may equalize between terminal ports only from point of origin, as provided and subject to the limitations set forth herein.¹ Equalization is the absorption by the carrier of the difference between shipper's cost of delivery to ship's tackle at Terminal Dock at nearest conference terminal port and the cost of delivery to ship's tackle at terminal dock and port of equalizing line. Conference terminal ports and docks are those named in Rule No. 5. Conditions and limitations as to equalization follow:

(a) Equalization shall not exceed an absorption in excess of 35 percent of the ocean freight, including handling charges and wharfage.

1. In the Pacific Straits Conference rule and the Pacific/Indonesian Conference rule, the following appears in lieu of the foregoing four sentences:

Rates are based on direct loading at loading port or docks, but the individual member line Carriers may meet the competition of other member lines loading direct at terminal ports or docks, either by transshipment or by equalization from point of origin.

Otherwise the rules of the three conferences are substantially the same, insofar as they relate to the Port of Stockton.

(b) A carrier may not equalize between terminal ports and non-terminal ports, or between non-terminal ports or between docks within a port.

(c) When the inland cost of transportation from point of origin is lower to terminal ports in Oregon, Washington, or British Columbia than via California terminal ports, equalization may be applied via California terminal ports only on shipments of deciduous fruits and dairy products (See Note below covering Explosives) and such equalization shall be permitted only so long as there is not adequate service from the terminal port in Oregon, Washington, or British Columbia, to which the cargo is tributary, to meet the needs of shippers of these commodities.

NOTE: Equalization on explosives is not permitted except that in the event a shipper is unable to obtain space for a specific shipment of explosives by a direct sailing from a terminal through which explosives would normally move at a date which reasonably will meet the needs of such shipper or his consignee, equalization shall be permitted on such shipment, Provided, that the shipper certifies to the Conference the need for space on such date and allows 48 hours after receipt of such certification for the Conference to indicate the conference carriers who can provide space on a direct sailing which reasonably will meet the shipper's needs.

(d) Equalization is permitted on shipments of fresh fruits, which would normally be shipped via California terminal ports when shipped via terminal ports in Oregon, Washington, or British Columbia, when there is not adequate service from the California port, to which the cargo is tributary, to meet the needs of shippers of these commodities.

(e) Cargo which would normally move from one terminal port in Oregon, Washington, or British Columbia, may be

shipped under equalization through another terminal port in Oregon, Washington, or British Columbia, and cargo which would normally move from one California terminal port, may be shipped under equalization via another California terminal port.

(f) Equalization shall only be paid on the basis of the lowest applicable common carrier or contract carrier rates.

(g) In support of each claim for equalization the shipper must furnish the carrier a copy of transportation bill covering movement from point of origin.

(h) Prior to payment of equalization bills, Carriers must submit to the Conference on prescribed form a certified statement for confirmation and approval of applicable interior rates and/or the basis for equalization.



FEB 14 1967

No. 20550 ✓

**United States
Court of Appeals
for the Ninth Circuit**

NATIONAL FARMERS UNION PROPERTY
and CASUALTY COMPANY,

Appellant,

vs.

LAURENCE COLBRESE, JR.,

Appellee.

On Appeal from the United States District Court
for the District of Montana.

Brief of Appellant

WIGGENHORN, HUTTON, SCHILTZ
& SHEEHY

403 Electric Building
Billings, Montana

Attorneys for Appellant

FILED

Filed _____, 1966

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WM. B. LUCK, CLERK

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1	1. The first part of the book is devoted to a general survey of the history of the world from the beginning of time to the present day.
2	2. The second part of the book is devoted to a detailed account of the history of the world from the beginning of time to the present day.
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20	20. The twentieth part of the book is devoted to a detailed account of the history of the world from the beginning of time to the present day.

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vs.

LAURENCE COLBRESE, JR.,

Appellee.

On Appeal from the United States District Court
for the District of Montana.

Brief of Appellant

B. *STATEMENT OF PLEADINGS AND FACTS DISCLOSING JURISDICTION.*

(a) Complaint (Tr., Vol. II, pp. 2-9) was filed in the District Court of the United States for the District of Montana, Billings Division, on September 25, 1963.

(b) The complaint alleges that the defendant National Farmers Union Property and Casualty Company is a capital stock corporation organized under the laws of the State of Utah, with its principal office in Denver, Colorado; plaintiff Laurence Colbrese, Jr., is a resident of the State of Montana. It is also alleged that the matter in controversy exceeds, exclusive of interest and costs, the sum of \$10,000 (Complaint, par. I, Tr., Vol. I, p. 2).

(c) The defendant appeared in the action and filed its answer to the plaintiff's complaint (Tr., Vol. I, pp. 10-14, inc.)

(d) Defendant in its answer admitted the jurisdictional allegations of diversity of citizenship and the jurisdictional amount (Answer, Second Defense, par. 3, Tr., Vol. I, p. 10).

(e) Under 28 U.S.C.A., Sec. 1332, the district courts have original jurisdiction of all civil actions where the matter in controversy exceeds the value of \$10,000, exclusive of interest and costs and is between citizens of different states.

(f) A jury trial was had between the parties as to one issue of fact, and the jury returned its answer to a

Special Interrogatory with respect to that issue of fact (Tr., Vol. I, p. 34). The Court subsequently entered written Findings of Fact and Conclusions of Law with respect to the whole of the case (Tr., Vol. I, pp. 55-62). Thereafter the Court, on September 7, 1965, rendered final judgment and decree in favor of appellee in the sum of \$18,862.88, with interest at 6% from October 16, 1962, and costs in the sum of \$136.70 (Tr., Vol. I, p. 79).

(g) Thereafter appellant filed a written Notice of Appeal with the clerk of the district court on October 5, 1965 (Tr., Vol. I, p. 81), and a bond for costs on appeal in the sum of \$500.00 (Tr. Vol. I, pp. 82-83). Said notice and bond were filed within thirty days of the judgment in accordance with Rule 73 of the Federal Rules of Civil Procedure.

(h) Also on October 5, 1965, appellant filed in the district court its written Statement of Points upon which it relied in this appeal (Tr., Vol. I, pp. 85-86) and its Designation of Record on Appeal (Tr., Vol. I, pp. 87-88), all as provided by Rule 75 of the Federal Rules of Civil Procedure.

(i) The appeal was filed in the United States Court of Appeals for the Ninth Circuit on November 15, 1965, and docketed on November 23, 1965.

(j) The jurisdiction of the said Court of Appeals depends upon Title 28, United States Codes, Section 1291, which provides that courts of appeal shall have

jurisdiction of appeals from all final decisions of the district courts of the United States; and upon Title 28, United States Codes, Section 2107, which provides that except as otherwise provided no appeal shall bring any judgment, order or decree before the court of appeals for review unless notice of appeal is filed within thirty days after the entry of such judgment, order or decree. The necessary steps were taken here to perfect the appeal.

(k) Original jurisdiction in the district court and the jurisdiction of this appellate court appear from the foregoing facts and the applicable statutes.

C. *STATEMENT OF THE CASE*

This appeal involves an incredible decision of the district court relating to the ownership of a 1949 Ford automobile that was involved in a fatal accident. The Ford was sold, or agreed to be sold, to Albert Kinney prior to September 2, 1958, by a Mrs. Robert McCormick.

Albert Kinney paid the full consideration for the Ford (Findings of Fact, Par. V, Tr., Vol. I, p. 56).

The only person who could claim adverse title to the Ford, Mrs. Robert McCormick, claims no title, and since September 2, 1958, thought that Albert Kinney was the owner of the Ford. (Request for Admissions, Par. 8, Tr., Vol. I, P. 16; admitted in Plaintiff's Answer to Request, Par. 3, Tr., Vol. I, P. 19.)

Albert Kinney took possession of the Ford, used it as his own for two years or more, and insured it as his own with appellant until September 3, 1960, when his insurance with appellant lapsed for non-payment of premium (Tr., Vol. I, p. 36).

Jerry Kinney, the 14-year-old son of Albert Kinney, and the driver involved in the fatal accident, used the Ford to hunt, to pick up companions, and to do farm chores (Tr. Vol. II, p. 35-40).

Nevertheless, the district court concluded that the Ford was a NON-OWNED AUTOMOBILE for Albert Kinney, and that it was NOT REGULARLY FURNISHED to Jerry Kinney at or prior to the fatal accident (Conclusions of Law, par. 2, Tr., Vol. I, p. 61).

The facts of the case, though somewhat involved, are fairly and concisely set forth in the Findings of Fact adopted by the court. The only real dispute between plaintiff and defendant is as to whether or not the Ford was "regularly furnished" to the driver at the time of the fatal accident, which was the subject of the jury trial and decision. We will set forth the essential facts here for the convenience of the court.

The 1949 Ford automobile was acquired by Albert Kinney when he purchased a farm and machinery and equipment thereon, including the Ford, from a Mrs. Robert McCormick prior to September 2, 1958, probably in the year 1957. The record owner of the farm and

the Ford was one C. W. Ehart, who had died prior to September 2, 1958, leaving as his sole heir one Robert McCormick. Upon Ehart's death McCormick became entitled to all of Ehart's right, title and interest in the Ford. Then Robert McCormick died, also prior to September 2, 1958, leaving as his sole heir Mrs. Robert McCormick, who thereupon became entitled to McCormick's right, title and interest in the Ford (Findings of Fact, Tr., Vol. I, p. 56, par. IV).

The Ehart estate is the subject of a probate proceedings in the appropriate district court in Yellowstone County, Montana. Certain of the probate papers are an exhibit in this case (Defendant's Ex. 12). Mrs. McCormick, as well as being the sole heir of the Ehart interest was also the administratrix of the Ehart estate on September 2, 1958, and prior thereto.

Prior to September 2, 1958, Mrs. McCormick agreed to sell all of her right, title and interest in the Ford to Albert Kinney for a consideration which has been fully paid. Since September 2, 1958, Kinney has been in possession of the Ford and has claimed to be its owner (Findings of Fact V, Tr., Vol. I, p. 56). Moreover, he thought himself to be the sole owner of all right, title and interest in the 1949 Ford (Defendant's Request for Admissions, par. 5, Tr., Vol. I, p. 16; admitted by plaintiff in Answer to Request for Admissions, par. 3, Tr., Vol. I, p. 19).

In addition, Mrs. Robert McCormick, from and since September 2, 1958, thought that Albert Kinney was the owner of all right, title and interest in and to the Ford (Defendant's Request for Admissions, par. 8, Tr., Vol. I, p. 16; admitted by plaintiff in Answer to Request for Admissions, par. 3, Tr., Vol. I, p. 19).

At the time of the transaction, Albert Kinney received the "Certificate of Registration and Tax Receipt" upon which licenses are issued in Montana, from Mrs. McCormick, and actually paid for the Montana licenses for the automobile for the years 1959 and 1960 (Findings of Fact, par. V, Tr., Vol. I, p. 56).

However, the "Certificate of Ownership" issued by the Registrar of Motor Vehicles of the State of Montana has not been delivered to Kinney by Mrs. McCormick or anyone else.

Albert Kinney requested of Thomas Bradley, Esq., the attorney representing Mrs. Robert McCormick in the transaction, and also representing the C. W. Ehart estate (Probate No. 10181 aforesaid) on four or five occasions for the title certificate of ownership to be issued to him; he made such request four or five times from the date of the transaction to December 3, 1960 (Defendant's Request for Admissions, par. 10, Tr., Vol. I, p. 17; admitted in Plaintiff's Answer to Request for Admissions, par. 3, Tr., Vol. I, p. 19).

On December 3, 1960, when Jerry Kinney, the minor

son of Albert Kinney was driving the Ford he ran off the highway on an icy stretch, upset, and thereby caused fatal injuries to the person of Duaine Colbrese, who was riding as a passenger in the Ford (Findings of Fact, No. III, Tr., Vol. I, p. 56). Laurence Colbrese, the appellee in this case, is the father of the deceased Duaine Colbrese.

At about the time that Albert Kinney acquired the Ford, he had procured a policy of insurance on it, from the defendant, covering the 1949 Ford and providing bodily injury liability and property damage coverages. Albert Kinney paid the defendant the insurance premiums due upon this policy for the years 1958 and 1959, but he allowed the policy to lapse for non-payment of premium on September 2, 1960. The said policy was lapsed and not in effect on the date of death of the minor, Duaine Colbrese, on December 3, 1960 (Findings of Fact No. XXV, Tr., Vol. I, p. 60).

At the time of the fatal accident, however, Albert Kinney had two other motor vehicles, one a 1951 Dodge passenger automobile, and the other, a 1954 International 1½ Ton Truck. Each of these vehicles were insured for bodily injury and property damage coverages with the appellant insurance company (Findings of Fact No. VI, VII, Tr., Vol. I, p. 57).

Thus, on the date of the fatal accident, December 3, 1960, Albert Kinney was the owner, or thought him-

self to be the owner of three vehicles, the Ford, the Dodge, and the International truck. Two of these were covered by insurance which Albert Kinney had procured, but the Ford was not covered by an insurance policy on it directly because Albert Kinney had let the insurance on that vehicle lapse.

Each of the insurance policies on the Dodge, and on the International Truck, contained the following provisions:

"A. Bodily injury, sickness or disease, including death resulting therefrom, hereinafter called bodily injury, sustained by any person * * *

arising out of the ownership, maintenance, or use of the owned automobile or any non-owned automobile * * *, and the company shall defend any suit alleging such bodily injury or property damage."

Other pertinent policy provisions were as follows:

"The following are insureds under (liability):

- (a) With respect to the owned automobile,
 - (1) the named insured and any resident of the same household;
 - (2) any other person using such automobile providing the actual use thereof is with the permission of the named insured;
- (b) With respect to a non-owned automobile,
 - (1) the named insured
 - (2) any relative, but only with respect to a private passenger automobile or trailer not regularly furnished for the use of such relative; * * *

"'Non-owned automobile' means an automobile or trailer not owned by the named

insured or any relative, other than a temporary substitute automobile."

(Findings of Fact, XIII, Tr., Vol. I, pp. 59, 60.)

From the foregoing quoted provisions of the insurance policies it is obvious, that since the 1949 Ford did not have insurance, the fatal accident in which it was involved would be covered by the other policies only if the 1949 Ford was a NON-OWNED AUTOMOBILE, and it was NOT REGULARLY FURNISHED for the use of Jerry Kinney, the driver at the time of the fatal accident.

Eventually suit was brought by the appellee, as father of the deceased Duaine Colbrese, against Jerry Kinney, the driver of the fatal Ford automobile. Kinney demanded that appellant appear and defend him in the suit. The appellant insurance company took the position that Albert Kinney owned this automobile, and that the automobile was regularly furnished to Jerry Kinney, and therefore declined to defend the suit or to admit coverage under the policies of the two other vehicles owned by Albert Kinney. A consent judgment was taken against Jerry Kinney and the judgment was satisfied upon assignment to the appellee of all rights of Jerry Kinney, to sue for and collect the indemnity from the appellant insurance company.

The District Court, incorrectly as we contend here, took the position that the title registration statutes in

Montana made the Ford automobile "non-owned" by Albert Kinney. The issue of whether the automobile was "regularly furnished" to Jerry Kinney was submitted to a jury for trial upon a special interrogatory. The jury returned its answer that it had not been regularly furnished to Jerry Kinney.

Judgment was entered against the appellant insurance company in the District Court and appellant appeals from that judgment here, principally upon the contention that it violates every tenet of common sense that under the facts here Albert Kinney was not the "owner" of the Ford automobile.

D. *SPECIFICATIONS OF ERROR*

Appellant specifies the following errors for consideration by the Circuit Court of Appeals:

1. It was error to deny appellant's Motions for Summary Judgment (Tr., Vol. I, p. 21 ; 45; Tr., Vol. II, p. 4).

2. It was error to enter judgment for appellee (Tr., Vol. I, p. 79).

3. The District Court erred in adopting its Conclusions of Law Nos. 2 and 3 as follows (Tr., Vol. I, p. 61):

"2. The 1949 Ford automobile in which plaintiff's son was killed was, on December 3, 1960, a "non-owned automobile" under defendant's insurance policies referred to in paragraphs VI and VII of the Findings of Fact, and was not regularly fur-

nished for the use of Jerry Kinney by his relative, Albert Kinney."

"3. Jerry Kinney was entitled to representation and defense of the lawsuit and claim made against him by Laurence Colbrese, Jr., in the state court action, and by refusing to so defend and represent Jerry Kinney, defendant breached the insurance contracts mentioned in paragraphs VI and VII of the Findings of Fact."

for the reason that under the facts, and the law, Albert Kinney was in fact the owner of the automobile, and the automobile was not a "non-owned automobile" under the insurance policies aforesaid.

4. The Court erred in refusing to adopt appellant's suggested Conclusion of Law No. 2 as follows:

"2. On December 3, 1960, Albert Kinney was the owner of and entitled to possession of said 1949 Ford." (Tr., Vol. I, p. 53)

for the reason that under the facts and under the law said Kinney was the owner of said Ford.

5. The Court erred in failing to adopt appellant's suggested Conclusion of Law No. 3 as follows:

"3. Because the certificate of ownership (certificate of title) of the 1949 Ford was then in the C. W. Ehart estate, Sec. 53-109(d) does not apply." (Tr., Vol. I, p. 53)

for the reason that under the facts and under the law the said subsection of the statute was inapplicable.

E. *ARGUMENT OF THE CASE*

Summary of Argument:

Subsection (d) of Sec. 53-109, R.C.M. 1947, does not

apply here. Since the paper title to the Ford was vested in the C. W. Ehart estate, Mrs. Robert McCormick, the seller of the Ford, as sole heir and as administratrix of the estate, could proceed to transfer title to the Ford under the provisions of subsection (e) of said Sec. 53-109, R.C.M. 1947. The punitive provisions of subsection (d) do not apply to procedures under subsection (e).

In the construction of statutes, such application of particular statutes as will give effect to the legislative intent, and yet be compatible and workable with other applicable statutes, without adding to or taking from the statutes, should be the objective of the court.

In the construction of contracts of insurance, terms used should be construed in their popular and ordinary sense, rather than according to their strict legal meaning.

Albert Kinney was the "owner" of the Ford under the definition of "owner" in Sec. 53-133, R.C.M. 1947.

The Sonnek and Safeco cases are declarations of the Montana Supreme Court for rescinded contracts of purchase of automobiles. In this case the contract of purchase is still fully in effect.

Therefore, even if subsection (d) of Sec. 53-109, R.C.M. 1947 would otherwise apply here, it has no application where the buyer of an automobile, the seller having failed to comply with the statute, has not rescinded the purchase of the Ford, especially as to a third party having no part in the contract of purchase. Where a buyer has accepted the benefits of a voidable contract for the purchase of a Ford, and has not acted to rescind the purchase, he should be held to be the owner as to those persons having no part in the contract.

The Questions Presented:

1. Do the punitive provisions of subsection (d) of 53-109, *Revised Codes of Montana 1947*, apply to a title certificate of ownership of an automobile where the person named in the title certificate is dead, and the sole heir or successor in interest of the dead person has transferred for a consideration which has been fully paid all of her interest in the automobile to a third person?

2. May not the heir or successor in interest, who has sold her interest in an automobile, proceed to transfer title to the buyer under subsection (e) of 53-109, R.C.M. 1947, without regard to subsections (a), (b), and (c) of that statute?

3. Are not the facts of the present case, involving a contract for the purchase of an automobile which is still fully in effect, distinguishable from the facts in the Montana cases of *Sonnek* and *Safeco*, which referred to rescinded contracts of purchase?

4. Is not the buyer of an automobile under a contract which has not been rescinded by him the "owner" of the vehicle under the definition of "owner" in subsection (f), *Sec. 53-133, R.C.M. 1947*, particularly where the buyer has the sole and exclusive possession of the automobile?

5. Should not the term "owner" under the facts in this case, be understood in its popular and ordinary sense, under *Sec. 13-710, R.C.M. 1947*?

It is conceded in this case that Mrs. Robert McCormick, the sole heir and the administratrix of the estate of C. W. Ehart has been fully paid for the Ford; she makes no claim to the Ford; she has fully surrendered its use and possession to Albert Kinney.

It is also conceded that Albert Kinney has had the use and possession of the automobile; he has exercised complete dominion over it; he has had exclusive possession for two and one-third years prior to the accident; he licensed the vehicle so that he could use it for two years; he fully paid for it; he insured it as his vehicle for two years; and at no time has he taken any steps to rescind his contract of purchase of the Ford in any particular.

How then did the District Court conclude that as far as Albert Kinney was concerned the Ford was a non-owned automobile at the time of the fatal accident?

Appellant contends that the intent and function of the *Revised Codes of Montana 1947, Sec. 53-109* was misapprehended in the court below; that particularly subdivision (d) of that statute was not applicable to the case at bar; that the construction given the statute by the lower court makes the statute unworkable; that the difference between a void and voidable contract was not appreciated and applied in the case; and that the underlying *rationale* of the decided cases in the state court per-

taining to the statute was not properly applied to the case at bar.

The statute involved, *Sec. 53-109* is long and complex; yet a thorough study of it is necessary to a complete understanding of the case at bar. We have set forth the entire statute at length in the appendix to this brief, both for the convenience of the court and so that the statute can be read in its entire context. We will, however, be referring to portions of that statute in this argument from time to time.

A short statement relating to the transfer of auto titles in Montana is perhaps in order. When a person in Montana buys a new car from a dealer or indeed a used car, or buys a car from a registered owner, the seller is required to write his signature with pen and ink upon the "Certificate of Ownership" issued for the auto on the reverse of the certificate, before a Notary Public. Within ten days the buyer or transferee must then forward the Certificate of Ownership together with the Certificate of Registration to the Registrar of Motor Vehicles who files the same. The Registrar then issues a new Certificate of Ownership and Certificate of Registration. Liens, mortgages or other encumbrances are shown on the Certificate of Ownership.

The foregoing statement is covered under the provisions of *53-109*, subsections (a), (b), and (c). We should state at this point that the "Certificate of Owner-

ship" is actually the paper title to the automobile. It is the indicia of ownership in the State of Montana. The "Certificate of Registration" to which we have referred is provided for in *Sec. 53-107, R.C.M. 1947* and is a separate slip of paper upon which a person applies for an automobile license from year to year in the State of Montana. The "Certificate of Registration" is not to be confused with the "Certificate of Ownership" which is the subject of the statute in question in the case at bar, *53-109, R.C.M. 1947*.

As we have said, the first three subsections of *Sec. 53-109* apply in the ordinary case of transfer of title to an auto, and compliance with those subsections is enforced by a quite stern provision in subsection (d) of the same statute, which provides as follows:

"Until said registrar shall have issued a certificate of registration and certificate of ownership and statement as hereinbefore provided, delivery of any motor vehicle shall be deemed not to have been made and title thereto shall not have passed and said intended transfer shall be incomplete and not be valid or effective for any purpose."

*Revised Codes of Montana, 1947,
Sec. 53-109 (d).*

The punitive effect of subsection (d), *supra*, has been applied in at least two Montana cases. They are as follows:

Sonnek v. Universal C.I.T. Credit Corporation,
374 P.2d 105, 108; 140 Mont. 503, 509.

Safeco Insurance Company of America v. Northwestern Mutual Insurance Company, 382 P.2d 174; 142 Montana 155.

In the *Sonnek* case, an automobile buyer brought an action in the Montana court to rescind the contract of purchase and a note and chattel mortgage executed by her in connection with the purchase on an automobile which she had bought from a dealer. She traded in a Chrysler automobile and paid some cash and executed a chattel mortgage to secure the balance of the purchase price. The mortgage form was prepared by Universal C.I.T. Credit Corporation and the mortgage was assigned to that corporation by the dealer.

The buyer had kept the automobile for a time, discovered that it was defective with a burned-out engine and took it back to the dealer. Upon this occasion the dealer agreed to take back the first car, sell her a second car, cancel the first mortgage on the first car, furnish 1959 license plates to the second car and transfer title to the second car to the buyer. The buyer surrendered possession of the first car and all papers in connection with this purchase. She executed a chattel mortgage on the second car for a purchase price which gave her credit for the down payment and the trade-in she had made. Once again the second mortgage was assigned to the credit corporation. She made some payments under the monthly installment requirement and on several occas-

sions demanded proper title papers for the second car. This title paper was never delivered to her.

As a result she was unable to obtain 1960 license plates for the second car and she discovered that the dealer did not cancel the mortgage on the first car. She thereupon notified the credit corporation by letter that she was rescinding the contract for the purchase of the second car and in her suit against the credit corporation and the dealer she demanded the return of what she had paid on the contract.

The credit corporation appeared in the action, claiming it was a holder in due course of the chattel mortgage, demanding the balance and the car or its value. The Montana court, in passing upon the case, held that there was a failure of consideration since the title did not pass to the buyer. It quoted subdivision (d) as we have set it forth above and held that since the provisions of 53-109 had not been complied with that title had not passed and there was no consideration for the note on which the chattel mortgage was based.

We point out specifically with respect to the *Sonnek* case that it did involve the ordinary purchase of an automobile by a buyer from a car dealer and the ordinary execution of chattel mortgages in connection with the purchase price. The dealer as seller did not comply with the provisions of 53-109 (a). Consequently she, as buyer, could not comply with the provisions of 53-109 (b) under

which she was to surrender the certificate to the Registrar of Motor Vehicles. Clearly here the Montana court was correct in deciding that there was a failure of consideration in that the title had not passed to her, and that she was entitled to rescind the purchase agreement.

It is also an important fact in the *Sonnek* case that the *buyer did in fact rescind* the agreement prior to the court's decisions.

We turn our attention now to the second case, that of *Safeco v. Northwestern Mutual Insurance Company, supra*.

In the *Safeco* case it appeared that on May 9, 1960, one Harlan Dean, the owner of a Hillman automobile, drove to Bearpaw Motor Company and tried out a Studebaker automobile. A price of \$350 plus the trade-in of the Hillman was discussed as the purchase price of the Studebaker. Harlan Dean left the Hillman with the dealer and drove away in the Studebaker, which he used in his work that day. On the following day, May 10, he told Bearpaw that he would take the Studebaker. He continued in possession of the Studebaker and on May 11 was involved in a serious accident.

No written agreements had been made in the *Safeco* case; the arrangements were all oral between Harlan Dean and Bearpaw Motor Company. The Certificate of Title to the Studebaker was never assigned by Bearpaw to Dean, nor was it ever delivered to him. In ad-

dition, there were no entries made in Bearpaw Motor Company's books as to whether a sale had been made, showing the price, the trade-in and the other pertinent data that would have gone into the records of the auto dealer. Moreover, Dean still kept the title to the Hillman automobile in his possession and it was never surrendered to the auto dealer. Subsequently Dean took the Hillman automobile back from the sales lot at Bearpaw and "the matter was at an end."

The *Safeco* case came to court because Safeco provided the liability insurance on the Hillman automobile and Northwestern Mutual Insurance Company provided liability under a garage owner's policy for the car dealer. A declaratory judgment was sought to have it judicially determined which company was primarily responsible for the defense of Harlan Dean and any liability imposed upon him as a result of the collision in the Studebaker.

Here again, in the *Safeco* case, the Montana court looked at the provisions of *Sec. 53-109*, and particularly to the provisions of subsection (d) of that statute and decided that since there was not a compliance with *Sec. 53-109* therefore title had not passed and the transfer was incomplete and not valid for any purpose.

It is important for the purposes of our discussion in this brief to keep in mind that in *Safeco* we were again involved with an ordinary transaction with a buyer going to a car dealer and either not actually entering into a con-

tract, or if one was entered into *it was certainly rescinded* because the buyer took his automobile back and "the matter was at an end" (382 P.2d 174, 177).

Probably the most important fact which differentiates the *Sonnek* and *Safeco* cases from the case at bar is that *Sonnek* and *Safeco* did actually involve the case of an ordinary transaction; but in this case, the case at bar, we have an entirely different situation. The owner of the paper title, the Certificate of Ownership, is C. W. Ehart, and he is dead.

The undisputed evidence here is that the Certificate of Ownership to the 1949 Ford was last listed under the name of C. W. Ehart (Stipulation, par. 3, Tr., Vol. I, p. 35). Moreover, his estate has not been fully probated, and no disposition of the Ford has been made in that estate; the last proceedings in the probate of the estate consisted of the filing of the Inventory and Appraisement which is a part of Exhibit 12 (Stipulation, par. 4, Tr., Vol. I, p. 35).

Does the fact that the owner named in the paper title is dead mean that the ownership of the Ford is suspended in some sort of legal limbo out of which it cannot be extracted? Not so; for the legislature has provided what should occur where the owner of the paper title dies and a transfer by operation of law has been effected. Subsection (e) of 53-109 provides in pertinent part:

"In the event of a transfer by operation of law of any title * * * of an owner of the legal title or owner in and to a motor vehicle registered under the provisions of this act, as upon inheritance, devise or bequest * * * the executor, administrator * * * or successor in interest of the person whose title or interest is so transferred shall forward to the Registrar of Motor Vehicles an application for registration in the form required for an original application of registration, together with a verified or certified statement of the transfer of such title or interest, which statement shall set forth the reason for such involuntary transfer, the title or interest so transferred, the name or names of the person or persons to whom such title or interest is to be transferred, the process of procedure effecting such transfer, and such other information as may be requested by the Registrar and with such statement shall be furnished such evidence and instruments as may otherwise be required by law to effect a transfer of legal or equitable title to or an interest in chattels as may be required in such cases, and in the event the registrar shall be satisfied that such transfer is regular and that all formalities as required by law have been complied with, he shall cause to be sent to the owner, conditional sales vendors, lessors, mortgagees and other lienors, as shown by his records, notice of such intended transfer and thereafter, but not less than five days thereafter, shall register such motor vehicle and shall issue a new Certificate of Ownership and Certificate of Registration to the person or persons entitled thereto * * *."

53-109 (e), R.C.M. 1947

Subsection (e), foregoing, by necessity provides the only means to transfer the paper title of an automobile where the owner named in the title paper has died before the transfer. Subdivision (e) is to be applied in those cases

not involving an ordinary transfer, as for example, a dealer to a buyer, or a live seller to a buyer, as these transfers are covered in subsections (a) and (b) of the statute.

Subsection (a) of the statute cannot apply in this case because subsection (a) requires that the owner named in the paper title sign the certificate with pen and ink. Obviously a dead person cannot comply with that provision.

We call attention particularly to those provisions in subdivision (e) of the statute, relating to transfers by operation of law, which provide that the executor, the administrator, "*or the successor in interest*" of the person whose title is transferred may forward to the registrar an application for registration.

We call attention to the fact that the application for registration is to be in the form required "for an original application of registration." Here again we have an important difference between the procedures provided under subsection (e) and those provided under subsections (a) and (b). In an ordinary transfer the certificate is merely forwarded with the endorsement thereon and a new title is issued (53-109 (a), (b), (c), R.C.M. 1947). But in an event such as this, where the owner named in the paper title is dead, an application of registration must be filed as for a brand new title. These provisions for application are found in *Sec. 53-106.1*,

R.C.M. 1947, but it is not important to set them forth here.

Subsection (e) of the statute, from its terms, would in this case allow the administratrix, Mrs. McCormick, or the buyer, Albert Kinney, as the "successor in interest" to make application for new title.

Moreover, the statute *does not require* in the event of a transfer by operation of law that the new title must be issued to the *direct successor of the transfer by operation of law*. Put another way, in this case subsection (e) does not require that application for a new title be made and that the only person who can get the new title is Mrs. Robert McCormick. That is not the purport of the statute. Rather, it is provided in subsection (e) that the statement accompanying the new application shall set forth (1) the reason for involuntary transfer; (2) the title transferred; (3) *the names of the persons to whom the title is to be transferred*; (4) *the process of procedure effecting such transfer*; (5) such instruments as may otherwise be required by law to effect a transfer of title and thereupon, (6) after proper notice to the parties the Registrar "shall issue a new Certificate of Ownership and Certificate of Registration *to the person or persons entitled thereto.*"

Under subsection (e) the power of the Registrar is not limited with respect to the transferee of the title. He can take into account "legal or equitable title," and upon

being furnished a statement as to whom the property is to be transferred must issue the certificate to that person. It is not necessarily the direct heir of the person who died. To read such a strict limitation into the provisions of subsection (e) is to put in the statute something that one does not find there from observation, taking it by its "four corners."

This point was completely missed by the District Court in construing the provisions of *Sec. 53-109*. That Court continued to believe that the transfer here had to occur under subsections (a), (b) and (c). In its "Discussion" in support of its Findings of Fact and Conclusions of Law the lower court stated that the "administrator of the estate, a Mrs. McCormick, should have taken proper steps under subsection (e) to obtain a certificate of ownership" but that the transfer from Mrs. McCormick "was a voluntary transfer governed by subsections (a), (b) and (d) of *Sec. 53-109*." In so stating, the court imposed a limitation upon subsection (e) that is not found in its language. The lower court did not take into account the words "successor in interest" which Albert Kinney certainly was.

In Montana, the construction of statutes is governed by the provisions of *Sec. 93-401-15, R.C.M. 1947*. That Section provides:

"Construction of statutes and instruments — general rule. In the construction of a statute or instrument, the office of the judge is simply to ascertain

and declare what is in terms or substance contained therein, not to insert what has been omitted, or to omit what has been inserted; and where there are several provisions or particulars, such a construction is, if possible, to be adopted as will give effect to all."

In the construction of a statute, the intent of the legislature is to be given effect (93-401-16, *R.C.M.* 1947). Moreover, in Montana, statutes and "all proceedings under them" are to be liberally construed with a view to effect their objects and to promote justice (*Sec. 12-202, R.C.M.* 1947). Again, all of the provisions of the codes are to be construed "as though all such codes had been passed at the same moment of time, and were parts of the same statute" (12-211, *R.C.M.* 1947).

Other code provisions which have a bearing and which ought to be taken into consideration in construing the provisions of 53-109 relate to the ownership of personal property. Some of those statutes are as follows (in all cases *Revised Codes of Montana, 1947*):

"67-201. (6663) *Property* — *what constitutes*. The ownership of a thing is the right of one or more persons to possess and use it to the exclusion of others. In this code the thing of which there may be ownership is called property."

"67-301. (6673) *Owner*. All property has an owner, whether that owner is the state, and the property public; or the owner an individual, and the property private. The state may also hold property as a private proprietor."

"67-303. (6675) *Ownership — absolute or qualified.* The ownership of property is either:

- (1) absolute; or
- (2) qualified."

"67-304. (6676) *When absolute.* The ownership of property is absolute when a single person has the absolute domain over it, and may use it or dispose of it according to his pleasure, subject only to general laws."

"67-305. (6677) *When qualified.* The ownership of property is qualified:

- (1) where it is shared with one or more persons;
- (2) when the time of enjoyment is deferred or limited;
- (3) when the use is restricted."

"67-315. (6685) *Present interest — to what entitles owner.* A present interest entitles the owner to an immediate possession of the property."

Construing the foregoing provisions with the provisions of 53-109, the title statute, it is certain that the 1949 Ford has to be owned by someone. "All property has an owner." It is obvious that the owner cannot be a dead person. Where a dead person is named on the title paper, his ownership transfers by operation of law, by bequest or inheritance. In this case his inheritance was to Robert McCormick. But Robert McCormick is also dead; he cannot be the owner. Mrs. McCormick is the "successor in interest" to the estate of Robert McCormick. She might be held to be the owner, but she has transferred her title, under the admitted facts in this case, to Albert Kinney, and has been fully paid for the transfer. It is obvious that in order to get the title

transferred the provisions of subsection (e) of 53-109 will have to prevail; it also ought to be obvious that the transfer can be effected to Albert Kiney under subsection (e) and a new certificate issued to him, without resort to the provisions of subsections (a), (b) and (c) of 53-109, the sections governing an ordinary transfer.

We turn our attention now to another important point in our presentation, the fact that the punitive provisions of subsection (d) of the statute do not apply to transactions under subsection (e) of the same statute.

Subsection (d) of the statute provides:

"(d) Until said Registrar shall have issued a certificate of registration and certificate of ownership and statement, *as hereinbefore provided*, delivery of any motor vehicle shall be deemed not to have been made and title thereto shall not have passed and said intended transfer shall be incomplete and not be valid or effective for any purpose." (Emphasis ours)

R.C.M. 1947, Sec. 53-109 (d)

By using the language "as hereinbefore provided" the legislature intends that the punitive effect of subsection (d) applies to transactions only under subsections (a), (b) and (c) of the same statute. And obviously because of the language "as hereinbefore provided," the punitive effect of the subsection does not apply to transfers which take place under subsection (e).

If it were not for the provisions of subsection (d), it would have to be admitted on all sides that there was in fact a completed contract of sale of personal property

in this case. Indeed the parties themselves thought so. Every aspect of a completed sale was present, unless the provisions of *Sec. 53-109 (d)* apply.

Sec. 67-1703, R.C.M. 1947, provides as follows:

"67-1703. (6879) *Transfer of title under sale.* The title to personal property, sold or exchanged, passes to the buyer *whenever the parties agree upon a present transfer*, and the thing itself is identified, whether it is separated from other things or not."
(Emphasis ours)

There is no doubt under the admitted facts in this case that as far as the parties themselves are concerned there had been a completed sale of the automobile.

Not only the grammatical reading of subsection (d), but also its history demonstrates that it was never intended that the provisions of subsection (d) should apply to procedures under subsection (e) of Section 53-109.

The first provision that we find in the Montana statutes relating to the registration of titles for motor vehicles is in the Session Laws of 1917. Under Chapter 75 of those Session Laws (*Laws of Montana, Fifteenth Session, 1917, Chapter 75*) the Secretary of State was constituted the Registrar of Motor Vehicles. Under Sec. 5 of that enactment owners were to file applications for registration. There was no provision in the act similar to subdivision (d) of the present 53-109.

The provisions of the 1917 enactment were carried into the 1921 Revised Codes of Montana and can be found distributed in three statutes with respect to regis-

tration, *Secs. 1757, 1758, and 1759 of the Revised Codes of 1921.*

A substantial change in the provisions for registration of motor vehicles was enacted in the Session Laws of 1933 (*Laws of Montana, Twenty-third Session, 1933*). It is in this enactment that one first finds provisions similar to our present statute, and in fact, the enactment in 1933 constitutes the basis for the present statute. This enactment was Chapter 159 of the Session Laws of 1933 and the provisions with respect to transfer of title or interest are found in subdivision 3 of that enactment. This subdivision 3, with minor amendments later enacted, constitute the basis for the present provisions of 53-109, *R.C.M. 1947.*

In looking at Subdivision 3 of Chapter 159 of the Session Laws of 1933, we find a subparagraph (a) requiring the "legal owner," that is the person whose title or interest is to be transferred, to write his signature with pen and ink upon the certificate of ownership. Subsection (b) provides within ten days thereafter the transferee shall forward the certificate to the registrar.

Subsection (c) provides that the provisions did not apply to the transfer of a motor vehicle to a dealer. Subsection (d) provided that the registrar upon receipt of a certificate of ownership properly endorsed would issue to the new owner a new certificate of registration and certificate.

It is in *subsection (e) of Chapter 159 of the Session Laws of 1933* that we find the provisions that are important in this case.

That subsection provided:

“(e) Until said registrar shall have issued said new certificate of registration and certificate of ownership, *as hereinbefore in subdivision (d) provided*, delivery of such vehicle shall be deemed not to have been made and the title thereto shall be deemed not to have passed and said intended transfer shall be deemed to be incomplete and not valid or effective for any purpose.” (Emphasis ours)

So it is clear that in the first enactment of this statute the provisions related specifically to subdivision (d) of the then enactment.

These provisions were carried into the *Revised Codes of Montana, 1935*, as *Sec. 1758.2*.

In 1943, in the Legislative Session of that year, this section was again amended (*Laws of Montana, Twenty-eighth Session, 1943, Chapter 148*). The principal effect of the amendment, as far as we are concerned, is that what had formerly been subdivisions (c) and (d) were combined in one section so that the new section (c) reads the same as the present (c) of Sec. 53-109 does now. It is important to note, however, that in the same enactment what was formerly subdivision (e) now became subdivision (d) and is as same as the present language in subsection (d) of 53-109. It is also important to note that in the 1943 enactment in subsection (d) the language “as hereinbefore provided” was continued.

Thus, the language of subsection (d) is now the same as it was enacted since 1943.

We point out, however, that in the 1933 enactment (Chapter 159, *supra*) where subdivision (e) said that the title was not effective unless the registrar issued a new certificate "as hereinbefore in subdivision (d) provided," the legislature also enacted subdivision (f) which is the same as the present subsection (e) of 53-109 relating to transfers by operation of law. The importance of this is that it shows the legislative intent that in those cases where there was a transfer by operation of law the provision that a transfer shall be deemed to be incomplete and not valid did not apply, by the terms of the specific statute. Again, in the 1943 amendment (Chapter 148, *supra*) when the former subdivisions (e) and (d) were combined, the language "as hereinbefore provided" was continued although the specific subsection was eliminated and immediately following the 1943 enactment is a provision with respect to transfers by operation of law. Again the intent of the legislature is clear: where transfers by operation of law are concerned, as in the case where the title is in an estate, there is no provision making transfers invalid in this situation and the legislature did not intend to make such transfers invalid where no certificate had been issued.

At the time of the transaction between Albert Kinney and Mrs. McCormick, she was a "successor in in-

terest" to the title which had transferred by operation of law, first to Robert McCormick, and then after his death to her. Therefore the correct procedure for her was outlined in subsection (e) of the statute and the punitive effect of subsection (d) does not apply.

When the lower court, in its "Discussion" (Tr., Vol. I, p. 64), states that the transfer by Mrs. McCormick to Kinney was a voluntary transfer governed by subsections (a), (b) and (c) of Sec. 53-109 it is asking for something that is presently unworkable. Mrs. McCormick is not a person who could transfer under the present provisions of 53-109 (a). She is not an "owner in or to a motor vehicle registered under the provisions of this act." The only provision of the registration statute which fits her situation is the provision in Sec. 53-109 (e) which would describe her as a "successor in interest of the person whose title or interest is so transferred." Therefore, any transfer by her is not subject to the punitive effect of subdivision (d) of the statute which relates only to transfers "as hereinbefore provided" and not to subsection (e).

What the Montana Court has stated in *State ex rel Hinz v. Moody*, 71 Mont. 473, 481, 230 Pac. 575, 578 (1924), has bearing here:

"The function of the courts is to interpret the law; that is, not to add to or take from the law, but to give effect to the intent expressed in the law itself. The object of construction as applied to a writ-

ten constitution is to give effect to the intent of the people in adopting it. In the case of all written laws it is the intent of the lawgiver that is to be enforced. But this intent is to be found in the instrument itself. It is to be assumed that language has been employed with sufficient precision to convey it, and unless examination demonstrates that the presumption does not hold good in the particular case, nothing will remain except to enforce it. "Where law is plain, and unambiguous, whether it be expressed in general or limited terms, the legislature should be intended to mean what they have plainly expressed, and consequently no room is left for construction." Possible or even probable meanings, when one is plainly declared in the instrument itself, the courts are not at liberty to search for elsewhere.' 'Whether we are considering an agreement between parties, a statute, or a constitution, with a view to its interpretation, the thing which we are to seek is the thought which it expresses. To ascertain this, the first resort in all cases is to the natural signification of the words employed, in the order of grammatical arrangement in which the framers of the instrument have placed them. If, thus regarded, the words embody a definite meaning, which involves no absurdity and no contradiction between different parts of the same writing, then that meaning, apparent on the face of the instrument, is the one which alone we are at liberty to say was intended to be conveyed. In such a case there is no room for construction. That which the words declare is the meaning of the instrument, and neither courts nor legislatures have a right to add to or take away from that meaning'. In interpreting clauses, we must presume that words have been employed in their natural and ordinary meaning (citing authorities).' Speaking in the same matter, Chief Justice Marshall says: The framers of the 'Constitution and the people who adopted it, must be understood to have employed words in their natural sense, and

to have intended what they have said (citing authority)'."

230 Pac., p. 578, 579.

The lower court apparently feels, from the language in its "Discussion" (Tr., Vol. I, p. 64) that in order to transfer the title here to Kinney, Mrs. McCormick, as administratrix of the estate, must first take steps under subsection (e) to obtain a certificate of ownership, presumably to Robert McCormick, since he is the person to whom the title transferred by operation of law upon the death of C. W. Ehart; then in the probate of the Robert McCormick estate take steps under subsection (e) to transfer the title to Mrs. McCormick as the sole heir of the decedent Robert McCormick; and then take steps under subsections (a), (b) and (c) of 53-109 as an ordinary voluntary transfer between herself and Mr. Kinney. We submit that this line of reasoning is an absurdity; that such procedures are not required; that it would result in an inordinate tie-up of the title to the Ford, and that the procedure outlined by statute under 53-109 (e) can accomplish the transfer from the C. W. Ehart estate to Albert Kinney without tying up the title in two estates.

The holding of the lower court in its "Discussion" (supra) seems to be at variance with its discussion in its first Memorandum Opinion (Tr., Vol. I, p. 40) wherein the lower court, in deciding the first Motion for Summary Judgment, stated:

"Subsection (e) prescribes the procedure to be followed by an executor, administrator, and others acting in a representative capacity, 'in the event of a transfer by operation of law or any title or interest of an owner of the legal title or owner in and to a motor vehicle registered under the provisions of this act, as upon inheritance, devise or bequest * * *'"

In a footnote to the foregoing quoted provision from the Memorandum Opinion the court also stated:

"1. In view of this statutory provision *there is no reason why the title certificate could not have been endorsed and delivered to Kinney prior to the completion of the Ehart and McCormick estates.*" (Emphasis ours)

(*Tr., Vol. I, p. 40*)

The lower court certainly was first under the impression that subsection (e) controlled the procedure to be followed in this case. We submit that the footnote in the first Memorandum Opinion correctly stated the possibilities under subsection (e) of the registration statute. If the procedure suggested in the footnote by the lower court had been followed, then by its terms, the punitive effect of subsection (d) would not apply since it has no relation to subsection (e).

In the foregoing portion of our brief we have been demonstrating that subsection (d) of the statute did not apply to the situation in the case at bar. But even if the provisions of subsection (d) did apply, the statute does not operate to make the contract of purchase between Albert Kinney and Mrs. McCormick void; rather what

existed between them was at most voidable if in fact subsection (d) did apply.

Albert Kinney never acted to rescind the contract in any particular for the purchase of the 1949 Ford. This fact is an important distinguishing feature that sets the case at bar apart from the factual situation in *Sonnek* and *Safeco*, in each of which cases there was an actual rescission of the agreement.

Subsection (d) does not purport to render the contract of purchase void. Rather it provides that if the certificate has not been issued the "title thereto shall not have passed and said intended transfer shall be incomplete and not be valid or effective for any purpose." (*Sec. 53-109 (d)*) In the terms of the statute it is an incomplete contract. The distinction between a "void" contract and a "voidable" contract is set forth in *American Jurisprudence 2d*:

"7. *Void, voidable, and unenforceable agreements.* There is an important distinction between "void" and "voidable" contracts, and confusion has resulted from the fact that a contract is sometimes said to be void when no more is intended than that it is voidable. A void contract is no contract at all; it binds no one and is a mere nullity. Accordingly, an action cannot be maintained for damages for its breach. No disaffirmance is required to avoid it, and it cannot be validated by ratification. A contract wholly void is void as to everybody whose rights would be affected by it if valid. Where one of two mutually dependent provisions of a contract is void, the parties are not bound by the other provision.

"A voidable contract, on the other hand, is valid and binding until it is avoided by the party entitled to avoid it. Furthermore, the defect therein may be cured by ratification by the party at whose instance it might have been avoided. The ratification may be express or implied — by express promise or by the conduct of the parties. If a party desires to rely upon the invalidity of a voidable contract, he must disclaim it and refuse to permit anything to be done under it insofar as it concerns him. However, the party to be charged with ratification of such a contract must have acted voluntarily with full knowledge of the facts * * *."

17 Am. Jur. 2d, 342, 343, Sec. 7, Contracts.

In *Grady v. City of Livingston*, (*Mont.*, 1943) 115 *Mont.* 47, 56, 141 P.2d 346, 350, our court stated that voidable contracts were not legally void and were not to be set aside or disregarded until they had been declared void by a court having jurisdiction. It further stated that a contract could be obviously void, but if the parties elect to proceed thereunder they may do so if no other parties are injured. It is conceded here that the parties elected to proceed under the contract even though it may have been voidable under the statute and certainly no third parties were injured by their so proceeding.

In *Parke v. Franciscus*, (*Calif.* 1924) 228 *Pac.* 435, 439, the California court construed a nearly identical statute to *Sec. 53-109 (d)*. There the California court said:

"The provision in question declares that until the transfer of the 'ownership' in the car has received the original certificate of registration and has writ-

ten his name upon the fact thereof in the blank space provided for that purpose by the department, the delivery of said motor vehicle shall be deemed not to have been made and title not to have passed, and said intended transfer shall be deemed to be incomplete and not to be valid or effective for any purpose. The provision does not make compliance therewith prima facie evidence of the ownership of the property in a car so registered and transferred, that is, the certificate of registration does not so declare it in terms. However, the words of the act are clear, plain and unambiguous and the meaning is not open to question. The failure of the transferee of the 'ownership' in the car to procure the registration certificate properly endorsed does not make the sale void ab initio, but in the terms of the statute it is incomplete. This interpretation of the intent of the legislature would seem to find support in the Motor Vehicle Act of 1923 * * *."

The holding in *Parke v. Franciscus* was concurred in *Kenney v. Christiansen*, 253 Pac. 715, 717 (1924) and in a long line of California cases where the rights of third parties were involved. The court has consistently protected such third parties although the original parties to the transaction have not complied with the registration requirements. See for example *Boles v. Stiles*, 204 Pac. 848; *Carpenter v. Devitt*, 122 P.2d 79; *Dennis v. Bank of America, Etc.*, 94 P.2d 51; *Willard H. George, Ltd., v. Barnett*, 150 P.2d 591; *Henry v. General Forming, Ltd.*, 200 P.2d 785.

By implication, the Montana Supreme Court has also found that in situations where the title statute has not been complied with, there is an incomplete contract,

or a voidable one, rather than one void *ab initio*. This is apparent from the *rationale* of the court set forth in the *Safeco* case in which the Montana Court said (332 P.2d 174, 179):

“* * * In any regular transaction the new certificate of ownership is required to be issued by the registrar and issues as a matter of course. *The transfer then becomes complete and valid and dates back to the time of the transfer between the parties.* If the transfer has not been made in compliance with the statute and the registrar by reason thereof does not issue a new certificate of ownership, clearly there was no transfer of ownership in its inception.” (Emphasis ours)

This language of the Montana Court in *Safeco* shows that the Montana Supreme Court does not regard the sale as void as a matter of fact, *ipso facto*. Rather, the situation is one of a voidable contract. Until one of the parties entitled to so act moves to set aside the voidable contract, the contract is binding as between the parties (*Grady v. City of Livingston*, 115 Mont. 47, 56; 141 P.2d 346, 350).

The difference between a void and a voidable contract is important in considering the decision of the late Judge Pray in Montana in *Firemen's Insurance Company of Newark, New Jersey, vs. Show*, 110 F. Supp. 523. In this case, decided before the *Sonnek* and *Safeco* cases, Judge Pray had before him a situation where Jerry Show bought a truck and took delivery of it on December 5 or 6 of 1950. Application was made to the Registrar

of Motor Vehicles for a certificate of title in his name and eventually it was received from the Registrar on December 20, 1950. In the meantime, on December 17, 1950, before the certificate of title had been issued, the truck was involved in an accident. The insurance company contended that because the certificate of title had not been issued on the date of the accident the seller, Perry Motors, was still the owner of the truck under *Sec. 53-109(d)*, and the insurance policy on Show never became effective. Judge Pray summarily disposed of this contention (110 F. Supp., p. 523) and pointed out that the insurance contract had been executed on November 29, 1950, and was in effect during the time that the application had been made for the certificate of title; and to hold for the insurance company in that instance would result in an option to the insurer to claim an alleged voidness or invalidity which would raise a cloud on every policy of automobile liability insurance. He rejected the contention as without merit.

Judge Pray's decision *on a contract fully in force* was cited to the Montana Court in the *Safeco* case, as the lower court noted, and it was not overruled specifically or by implication. Rather *Safeco* and the *Firemen's Insurance Company* case confirm what we contend, that involved here is a voidable contract rather than a void contract and that as between the parties Albert Kinney and Mrs. McCormick, Albert Kinney was the owner of

the automobile and would continue to be the owner until such time as he took steps to rescind the contract.

In this connection it should be noted that Albert Kinney did in fact demand that the title certificate be delivered to him. He made request for the title on four or five occasions after the purchase up to the time of the fatal accident.

The appellant insurance company, of course, had no part in the proceedings relating to the procurement of the certificate of title. This was entirely between Albert Kinney and Mrs. McCormick. Yet it is being penalized, under the decision of the lower court, for the inaction of the parties in obtaining the certificate of title. This was frowned upon by this Circuit Court in *Yoshida v. Liberty Mutual Insurance Company*, 240 F.2d 824, 828. Indeed, this court pointed out in that case something that is true in this case, that in the construction of contracts, including insurance policies, the provisions of a California statute, which are identical to a Montana statute, should be considered. The Montana statute is *Sec. 13-710, R.C.M. 1947*, which provides as follows:

"13-710. (7535) *Words to be understood in usual sense.* The words of a contract are to be understood in their ordinary and popular sense, *rather than according to their strict legal meaning*, unless used by the parties in a technical sense or unless a special meaning is given to them by usage, in which case the latter must be followed." (Emphasis ours)

It also provided in *Sec. 53-133, R.C.M. 1947* that

the definition of an "owner" of a motor vehicle is "any person, firm, association or corporation owning or renting a motor vehicle, or having the exclusive use thereof, under lease or otherwise, and shall also include a contract vendee."

We have here a case where the Montana Supreme Court has not spoken on the precise facts here in dispute. It has not had before it a situation where the title was vested in an estate, and has had no chance to speak out as to what the proper procedure should be.

Under *Erie Railroad Company v. Tompkins*, 58 S. Ct. 817, 304 U.S. 64, 82 L. Ed. 1188 a decision of the state court on the precise point in controversy is binding on the federal court.

Where the state court has not passed specifically on the question, or where a direct expression by the state court is lacking, then the federal court may have regard for any persuasive data available, such as compelling inferences or logical implications or other related adjudications and applicable statutes. Moreover, the federal court may resort to the rationale of the rule laid down by the state court in its decided cases which approach the question (*Spilberger v. Textron, Inc. (C.A., New York)* 172 F.2d 85). Indeed under *West v. American Tel. & Tel. Company*, 311 U.S. 223, 61 S. Ct. 179, 85 L.Ed. 139, federal courts, in cases such as this where the state court has not pronounced on the precise subject,

should ascertain from all other available data what the state law is, and apply that law.

“* * * In other words this court must endeavor to ascertain what decision the Montana Supreme Court would reach were the question presented to it.”

Duffy v. Lipsman-Fulkerson & Co.,
200 F. Supp. 71, 72 (U.S.D.C.,
Mont., 1961)

Thus far the Montana Court has not passed upon the question of ownership under an unrescinded contract for purchase of an automobile; it has not passed upon the bearing of the definition of “owner” found in *Sec. 59-133, R.C.M. 1947*; it has not passed upon the procedure for obtaining certificate of title under subsection (e) of *53-109, R.C.M. 1947*.

F. CONCLUSION

Once in a speech before a bar meeting, a member of this court stated that the function of an appellate court is “to make sure that the right party wins the lawsuit.”

Here is a case where the buyer of an automobile took possession of the automobile, exercised complete dominion over it for two and a third years until the fatal accident, has never surrendered it, caused it to be licensed for two years, insured it as his own for two years, paid for it, and “figured it was his.” Yet, he has been held here not to be the “owner” of the automobile.

Such a decision is incongruous and manifestly unjust, and we ask reversal by this court.

Dated, Billings, Montana,
January 21, 1966.

Respectfully submitted,

WIGGENHORN, HUTTON,
SCHILTZ & SHEEHY

By JOHN C. SHEEHY
Attorneys for Appellant

CERTIFICATE

John C. Sheehy, an attorney duly authorized to practice in the United States Court of Appeals for the Ninth Circuit states as follows:

I certify that, in connection with the preparation of this brief, I have examined Rules 18 and 19 of the United States Court of Appeals for the Ninth Circuit, and that, in my opinion, the foregoing Brief is in full compliance with those rules.

JOHN C. SHEEHY
Attorney for appellant

ACKNOWLEDGEMENT OF SERVICE

Due service of the within and foregoing Brief of Appellant, and receipt of 3 copies thereof, made and admitted this 21st day of January, 1966.

CROWLEY, KILBOURNE, HAUGHEY,
HANSON & GALLAGHER

By LOUIS R. MOORE
Attorneys for Appellee

APPENDIX

1. *Full text of Sec. 53-109, R.C.M. 1947:*

"53-109. (1758.2) *Transfer of title or interest.* (a) Upon a transfer of any title or interest of an owner or owner in or to a motor vehicle registered under the provisions of this act as hereinbefore required, the person or persons whose title or interest is to be transferred shall write their signatures with pen and ink upon the certificate of ownership issued for such vehicle, in the appropriate space provided upon the reverse side of such certificate, and such signature shall be acknowledged before a notary public.

(b) Within ten (10) days thereafter, the transferee shall forward both the certificate of ownership so endorsed and the certificate of registration together with the information required under section 53-107, to the registrar, who shall file the same upon receipt thereof, and no certificate of ownership and certificate of registration shall be issued by the registrar of motor vehicles until the outstanding certificates are surrendered to that office or their loss established to his reasonable satisfaction.

(c) The provisions of subdivision (b) of this section, requiring transferee to forward the certificate of ownership after endorsement and the certificate of registration to the registrar, shall not apply in the event of the transfer of a motor vehicle to a duly licensed automobile dealer intending to resell such vehicle and who operates the same only for demonstration purposes, but every such dealer shall upon transferring such interest deliver such certificate of ownership and certificate of registration with an application for registration executed by the new owner in accordance with the provisions of section 53-107, and the registrar upon receipt of said certificate of ownership, certificate of registration and application for registration, together with the conditional sales contract or other lien, if any, shall issue a new certificate of ownership and certificate of registration together with a statement of any conditional sales contract, mortgage, or other lien as provided in said section 53-107.

(d) Until said registrar shall have issued a certificate of registration and certificate of ownership and statement as hereinbefore provided, delivery of any motor vehicle shall be deemed not to have been made and title thereto shall not have passed and said intended transfer shall be incomplete and not be valid or effective for any purpose.

(e) In the event of a transfer by operation of law of any title or interest of an owner of the legal title or owner in and to a motor vehicle registered under the provisions of this act, as upon inheritance, devise or bequest, order in bankruptcy or insolvency, execution sale, repossession contract, or otherwise than by voluntary act of the person whose title or interest is so transferred, the executor, administrator, receiver, trustee, sheriff or other representative, or successor in interest of the person whose title or interest is so transferred shall forward to the registrar of motor vehicles an application for registration in the form required for an original application for registration, together with a verified or certified statement of the transfer of such title or interest which statement shall set forth the name or names of the person or persons to whom such title or interest is to be transferred, the process of procedure effecting such transfer and such other information as may be requested by the registrar and with such statement shall be furnished such evidence and instruments as may otherwise be required by law to effect a transfer of legal or equitable title to or an interest in chattels as may be required in such cases, and in the event the registrar shall be satisfied that such transfer is regular and that all formalities as required by law have been complied with, he shall cause to be sent to the owner, conditional sales vendors, lessors, mortgagees and other lienors, as shown by his records notice of such intended transfer and thereafter, but not less than five (5) days thereafter, shall register such motor vehicle and shall issue a new certificate of ownership and certificate of registration to the person or persons entitled thereto. The notice herein required shall be deemed complied with by deposit in the post office in Deer Lodge, Montana, such notice,

postage prepaid, addressed to such person or persons at the respective addresses shown on his records.

In the event of the death of an owner of one or more motor vehicles and/or trailer, and/or semitrailer, and/or trailer-house registered hereunder and not exceeding the value of one thousand dollars (\$1,000.00), without leaving other property necessitating the procuring of letter of administration or letters testamentary then the surviving husband or wife, or other heir, unless such property is by will otherwise bequeathed, may secure transfer of the certificate of ownership and the certificate of registration of the deceased, in and to such motor vehicle in the name of the surviving husband or wife or other heir, as above mentioned, upon filing with the registrar an affidavit of such person setting forth the fact of survivorship and the name and address of any other heirs and such other facts as are hereby made necessary to entitle the affiant to a transfer and thereupon the registrar is authorized to make such transfer of the certificate of ownership and certificate of registration, subject to all contracts, leases, mortgages, or other liens as shown by his records.

Nothing in the foregoing subdivision of this section shall prevent any conditional sales vendor, mortgagee, or other lienor from assigning his interest or title in or to a motor vehicle registered under the provisions of this act to any other person without the consent of and without effecting the interest of the holder of the certificate of ownership and certificate of registration. Upon any conditional sales vendor, mortgagee, or other lienor assigning his interest in any motor vehicle registered under this act a copy of such assignment must be filed with the registrar and record thereof made upon his records.

(f) Every person who transfers any motor vehicle to a junk dealer for the purpose of scrapping said vehicle shall so notify the registrar and deliver the certificate of ownership and certificate of registration to the registrar for cancellation."

*Revised Codes of Montana, 1947,
Sec. 53-109.*

2. *List of Exhibits:*

Plaintiff's (Appellee's) Exhibits:

1. Insurance policy No. A24-030,461;
Intl. 12/58 to 6/59.
2. Insurance policy No. A24-107; 394;
Dodge 9/59 to 3/60.
3. Assignment
4. Ratification of assignment.
5. Dodge period coverage.
6. Intl. period coverage.
7. 1955 Ford application.
8. Dodge application.
9. Intl. application.
10. Certificate of title and letter.

Defendant's (Appellant's) Exhibits:

11. Copy of policy coverage.
12. Probate photostats.
13. 1949 Ford application
14. Colbrese v. Kinney court file.
15. Copy of Stipulation.

All admitted by stipulation at pretrial conference.

FEB 14 1967
No. 20550

United States Court of Appeals for the Ninth Circuit

NATIONAL FARMERS UNION PROPERTY
and CASUALTY COMPANY,

Appellant,

vs.

LAURENCE COLBRESE, JR.,

Appellee.

On Appeal from the United States District Court
for the District of Montana.

Brief of Appellee

WIGGENHORN, HUTTON,
SCHILTZ & SHEEHY

403 Electric Building

Billings, Montana

Attorneys for Appellant

CROWLEY, KILBOURNE, HAUGHEY,
HANSON & GALLAGHER

500 Electric Building

P. O. Box 2529

Billings, Montana

Attorneys for Appellee

Filed _____, 1966

FEB 14 1967

_____, Clerk

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On Appeal from the United States District Court
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Brief of Appellee

STATEMENT OF THE CASE

We agree with appellant that this court has jurisdiction. The facts are completely and accurately stated by the District Court in its Findings of Fact (Tr., Vol. I, p. 55, et seq), and in the District Court's "Memorandum Opinion" on the motion for summary judgment (Tr., Vol. I, p. 37, et seq). The brief of appellant does not in some respects present accurately and fairly the evidence as it actually exists in the record. Despite some repetition appellee will summarize the facts for the convenience of the Court.

On December 3, 1960, Duaine Colbrese, son of plaintiff Laurence Colbrese, Jr., was riding as a passenger in a 1949 Ford sedan, driven by Jerry Kinney, on U. S. Highway #10 at a point approximately one mile east of Reedpoint, Montana, when the automobile skidded on ice, left the highway, upset and caused injuries to Duaine Colbrese which resulted in his death. At the time of his death, Duaine Colbrese was 16 years of age. (Complaint, Par. II & III; Admitted in Answer, Par. 3).

The ownership of the 1949 Ford is treated separately hereafter, (p. 7), but suffice it to say at this point that registered title was in one C. W. Ehart, who had died previous to December 3, 1960. (Tr., Vol. I, p. 38)

At the time of the accident, the Ford was not cover-

ed by an insurance policy listing it as the insured vehicle. However, on and prior to December 3, 1960, Albert Kinney, the father of Jerry Kinney, owned two other vehicles (a 1951 Dodge automobile and a 1954 International 1½-ton truck), both of which were insured by the appellant insurance company under policies listing Albert Kinney as the named insured (Exhibits 5 & 6), providing for bodily injury liability coverage, property damage coverage, and medical payments coverage, (Tr., Vol. I, p. 57). These policies also provided coverage of any relative of the named insured while using any "non-owned" automobile, provided the "non-owned" automobile was not regularly furnished for the use of such relative, (Tr. Vol. I, p's 59, 60).

On May 26, 1961, Laurence Colbrese, Jr., appellee herein, filed an action in the District Court of the Thirteenth Judicial District of the State of Montana, in and for the County of Yellowstone, in which Laurence Colbrese, Jr., was plaintiff and Jerry Kinney was named defendant, wherein Colbrese prayed for judgment and damages in the total sum of \$40,850.00, including, as special damages, the sum of \$850.00 as casket, funeral and cemetery expenses. (Tr., Vol. I, p. 57)

After the action was filed, Albert Kinney, as father of Jerry Kinney, made written demand upon appellant that it appear and defend said action on behalf of Jerry

Kinney. Appellant declined to accept the defense of the action and declined to admit coverage under any of the policies theretofore issued to Albert Kinney. (Complaint, Par. VIII, admitted by Answer, Par. 7, Tr., Vol. I, p's 4, 10)

After a change of venue, in the Montana District Court proceedings, from Yellowstone County to Stillwater County, Montana, an offer of compromise was made by Jerry Kinney, through his guardian ad litem, Albert Kinney, for judgment to be taken against Jerry Kinney in the sum of \$18,850.00. This offer of judgment was accepted by Laurence Colbrese, Jr., and judgment was entered on October 16, 1962, in the said amount, together with costs in the sum of \$312.88, making a total judgment of \$18,862.88. (Tr., Vol. I, p. 58)

After entry of said judgment, Jerry Kinney, acting through his attorney, made demand upon appellant in writing for payment of the said judgment. The defendant declined to accept liability for the judgment under any of its policies of insurance. (Tr., Vol. I, p. 58)

On June 7, 1963, Albert Kinney was appointed by the District Court of the Thirteenth Judicial District, in and for the County of Yellowstone, as guardian of Jerry Kinney, and letters of guardianship were issued to him on June 7, 1963. On the same day, Albert Kinney, as guardian, petitioned the Court for an order au-

thorizing him to execute for his ward an assignment of Jerry Kinney's right to sue for and collect indemnity from appellant in the amount of the judgment entered against it, plus attorneys' fees, in consideration of satisfaction of the judgment by Laurence Colbrese, Jr. On said date, an order was entered by the presiding Judge in the State District Court authorizing the guardian to execute such an assignment in consideration of such satisfaction. The assignment was executed on June 12, 1963, the judgment satisfied, and Colbrese has brought the present action on the basis of the said assignment. (Tr., Vol. I, p. 59)

As stated above, at the time and place of the accident hereinabove referred to, the 1949 Ford was registered, with the State Registrar of Motor Vehicles of the State of Montana, in the name of C. W. Ehart. No "Certificate of Ownership" (title) to said motor vehicle has ever been issued to anyone other than C. W. Ehart since the date of the accident. (Tr., Vol. I, p. 56)

The primary question submitted for decision of the trial court was whether the 1949 Ford, as operated by Jerry Kinney, was covered under the "non-owned" automobile" provisions of the insurance policies issued to Albert Kinney by appellant on the Dodge automobile and International truck.

Each of the insurance policies required the appel-

lant to pay on behalf of "the insured" all sums which the insured should become obligated to pay as damages because of:

"A. Bodily injury, sickness or disease, including death resulting therefrom, hereinafter called bodily injury, sustained by any person * * *

"Arising out of the ownership, maintenance or use of the owned automobile or any non-owned automobile * * *."

The following are listed as insureds under the liability portions of the policies:

"(a) With respect to the owned automobile,

(1) the named insured and any resident of the same household.

(2) any other person using such automobile, provided the actual use thereof is with the permission of the named insured;

(b) With respect to a non-owned automobile,

(1) the named insured,

(2) any relative, but only with respect to a private passenger automobile or trailer not regularly furnished for the use of such relative; * * *

" 'Non-owned automobile' means an automobile or trailer not owned by the named insured or any relative, other than a temporary substitute automobile; "

(Tr., Vol. I, p's 59, 60)

The issue of ownership was first presented to the trial court on a motion for summary judgment filed by appellant, which was denied, (Memorandum Opinion,

Tr., Vol. I, p. 37, et seq). In his memorandum opinion denying the motion for summary judgment, Judge Jameson held that the 1949 Ford was a "non-owned automobile" by reason of the fact that no "certificate of ownership" (title) ever was issued to Albert Kinney in compliance with the provisions of *Sec. 53-109, R.C.M. 1947*, (Tr., Vol. I, p. 39), relying upon *subsection (d) of Sec. 53-109*, and the case of *Safeco Ins. Co. v. Northwestern Insurance Co.*, (1963) 142 Mont. 155, 382 P.2d 174.

After appellant's motion for summary judgment was denied, two trials were held, the first with an advisory jury, (Tr., Vol. II), on the question of whether the Ford had been regularly furnished for the use of Jerry Kinney (the jury found that the Ford had not been regularly furnished for his use) (Tr., Vol. I, p. 34); and a second trial, before the Court, on all other defenses raised by appellant. (Tr., Vol. III) After submittal of briefs by the parties, the Court adopted its Findings of Fact and Conclusions of Law. (Tr., Vol. I, p. 55) This appeal followed.

FACTS RELATING TO OWNERSHIP

The facts, as to ownership of the Ford, can be stated as follows:

In 1957, Albert Kinney purchased a small ranch near Laurel, Montana, with all machinery thereon, from one Mrs. McCormick, the heir of the original owner,

C. W. Ehart. Parked on the ranch was a 1949 Ford sedan with a broken "rear end", (Tr., Vol. II, p. 10), registered in the name of C. W. Ehart. Both Mrs. McCormick and Albert Kinney thought this Ford was included in the sale of the ranch and machinery, and Mrs. McCormick gave Albert Kinney the keys and registration certificate (enabling the possessor to purchase a license for the auto), but no "certificate of ownership" (title) was executed or transferred to Kinney. (Finding of Fact V, Tr., Vol. I, p. 56)

About August 27, 1958, Kinney had the "rear end" repaired, (Tr., Vol. II, p. 20) and started using the car. Shortly thereafter (on September 2, 1958, Tr., Vol. II, p. 10), he procured insurance thereon from appellant (Finding of Fact XV, Tr., Vol. I, p. 60), fully advising the insurance company's agent that he had not received the ownership certificate. (Finding of Fact XVI, Tr., Vol. I, p's 60 & 61) The insurance was kept in force until September 3, 1960, at which time Kinney declined to renew it for the following reasons (in his words):

"Well, I had given up on getting title to the car and it had quit running. I figured it would be just foolish for me to fix it up, not being able to get title, so I just parked it and just let the insurance lapse."

(Tr., Vol. II, p. 11)

Then approximately 3 weeks before the accident,

(Tr., Vol. II, p. 12), Albert Kinney's son-in-law, home on furlough from the Navy, fixed the Ford and Albert Kinney used it "a time or two" from that time until the day of the accident. (Tr., Vol. II, p's 18, 19) At no time did Mrs. McCormick comply with the title registration statutes of Montana, although Kinney, on four or five occasions, requested the attorney handling the Ehart estate proceedings to furnish a "certificate of ownership" (title) on the Ford. (Finding of Fact No. V, Tr., Vol I, p. 57)

ARGUMENT ON THE ISSUE OF OWNERSHIP SUMMARY:

1. THE 1949 FORD AUTOMOBILE WAS A "NON-OWNED" AUTOMOBILE WITHIN THE MEANING OF ALBERT KINNEY'S INSURANCE POLICY BY REASON OF THE FACT THAT NO CERTIFICATE OF OWNERSHIP EVER WAS ISSUED TO KINNEY IN COMPLIANCE WITH *SECTION 53-109, R.C.M. 1947*.

ALBERT KINNEY COULD HAVE ACQUIRED TITLE OR OWNERSHIP OF THE 1949 FORD ONLY BY TRANSFER.

SUBSECTIONS (a) AND (b) OF SEC. 53-109, R.C.M. 1947 PROVIDE THE SOLE PROCEDURE FOR EFFECTING A VOLUNTARY TRANSFER OF A MOTOR VEHICLE FROM ONE PERSON TO ANOTHER.

FAILURE TO COMPLY WITH THE ABOVE SUBSECTIONS PRECLUDED THE ATTEMPTED TRANSFER FROM BECOMING EFFECTIVE FOR ANY PURPOSE, *SEC. 53-109(d), R.C.M. 1947.*

SINCE THERE WAS NO COMPLIANCE WITH SUBSECTIONS (a) AND (b), NO TRANSFER FROM MRS. McCORMICK TO ALBERT KINNEY WAS EVER ACCOMPLISHED AND ALBERT KINNEY WAS NOT THE "OWNER" OF THE 1949 FORD.

"NON-OWNED" WAS DEFINED IN THE INSURANCE POLICIES MERELY AS "NOT OWNED BY THE NAMED INSURED," NO DEFINITION OF "OWNED" BEING SUPPLIED. SINCE "OWNED" IS A GENERIC AND GENERAL TERM AND THUS AMBIGUOUS, IT MUST BE CONSTRUED IN ACCORDANCE WITH THE GENERAL LAW AND STATUTES OF MONTANA, AND ANY UNCERTAINTY RESULTING FROM FAILURE TO DEFINE THE WORD IN THE POLICY MUST BE RESOLVED IN FAVOR OF THE INSURED. THIS PRECLUDES ANY ATTEMPT BY THE INSURER TO DEFINE "OWNED" AS BEING EQUITABLE, QUALIFIED OR ANYTHING

LESS THAN THE RECORD OWNERSHIP PROVIDED BY THE MOTOR VEHICLE REGISTRATION STATUTES.

Albert Kinney never obtained a certificate of ownership of the 1949 Ford, nor was such a certificate ever issued to him. At all times pertinent to this case, the said automobile was registered to C. W. Ehart. *Subsection (d) of 53-109, R.C.M. 1947* provides:

"(d) Until said registrar shall have issued a certificate of registration and certificate of ownership and statement as hereinbefore provided, delivery of any motor vehicle shall be deemed not to have been made and title thereto shall not have passed and said intended transfer shall be incomplete and not be valid or effective for any purpose."

Subsections (a) and (b) were never complied with. Therefore, subsection (d) compels the conclusion that the intended transfer to Albert Kinney was not *valid or effective for any purpose*. Thus, the 1949 Ford was a "non-owned" automobile covered by Albert Kinney's insurance policies. District Judge W. J. Jameson so held following the language of the statute as it was interpreted in *Safeco*. (*Safeco Ins. Co. of America v. Northwestern Mutual Ins. Co.*, (1963) 142 Mont. 155, 382 P.2d 174.)

The *Safeco* case was a declaratory judgment action to determine which of two insurance companies was primarily responsible for the defense of one Harlan

Dean and any liability imposed upon him for an accident which occurred when Dean was driving a 1958 Studebaker car which he had procured from a used car lot in Havre, Montana, in trade for a Hillman automobile owned by him. Safeco Insurance Company carried the liability insurance on the Hillman automobile or any "owned" replacement and Northwestern Mutual Insurance Company carried liability insurance on the used car dealer. (Tr., Vol. I, p. 40)

The trial court in the *Safeco* case found that there had been a completed sale even though the requirements of the motor vehicle registration statutes of Montana (*Sec. 53-109, et seq*) had not been complied with, and thus that the Studebaker was no longer owned by the used car dealer but was owned by Dean and covered by the Safeco policy on the Hillman as a replacement automobile. (Tr., Vol. I, p. 40)

On appeal, the plaintiff-appellant in the *Safeco* case contended that motor vehicles could be transferred as to ownership only by endorsement of the title as required by *subdivision (a) of Sec. 53-109, R.C.M. 1947*, and that under *subsection (d)* of the same statute, delivery, passing of title, or the transfer of any interest in the automobile could not be valid or effective for any purpose without compliance with such statute. (*382 P.2d at 176*)

The Supreme Court of Montana agreed with the

plaintiff-appellant and reversed the District Court; holding that no attempt having been made by the parties to the transaction to comply with *Sec. 53-109*, there never was a completed sale. The Court also stated that the provisions of the Motor Vehicle Code provided that exclusive method of accomplishing a valid sale and transfer of a motor vehicle in Montana. (382 P.2d, 179)

In the instant case, Judge Jameson obtained and examined the briefs of all parties to the *Safeco* case, including one filed by amicus curiae (Tr., Vol. I, p. 41) and concluded that the *Safeco* case was in point on the critical aspects and bound him. (Tr., Vol. I, p. 78)

By the *Safeco* case, we submit, the Montana Supreme Court has ruled once and for all that, in Montana, the title registration statutes are the exclusive method of accomplishing a valid sale and transfer of a motor vehicle, and thus that no set of circumstances falling short of compliance with the statute can result in a completed sale.⁽¹⁾ As applied to the case at bar, the failure of Mrs. McCormick and Albert Kinney to comply with the provisions of (*Sec. 53-109*) preclude Kinney from being considered the "owner" of the Ford, under the policies involved.

The attempted transfer here was from an heir, (Mrs.

(1) This holding was recently followed by the Montana Supreme Court. *Interstate Manufacturing Co. vs. Interstate Products Co.* (1965) Mont., 408 P.2d 478.

McCormick) without "title" in her name to a third person (Albert Kinney). Under these circumstances, Mrs. McCormick could not have transferred the "title" to Albert Kinney until she obtained a "title" herself. We believe, and the District Court held, (Tr., Vol. I. p's 40 and 64), that Mrs. McCormick could have acquired a "title" by complying with *subsection (e)* of *Sec. 53-109* and then could have (and should have) signed the "title" and given it to Albert Kinney as required by *subsection (a)*. Albert Kinney then should have forwarded it to the Registrar of Motor Vehicles as provided by *subsection (b)*. Failing in this, no title passed to Albert Kinney for any purpose, because of *subsection (d)* of *Sec. 53-109*.

Another reason why definition of the words "non-owned" in the insurance policies involved in this litigation should be held to include the 1949 Ford is that the words "non-owned" are not accurately defined in the policies. If appellant had so desired, it could have defined the words to include the qualified or equitable claim to ownership it asserts here. Appellant could have changed the meaning of the words "non-owned" to exclude vehicles which were not owned but used by the insured for any period of time whatever, but did not do so. It also could have defined the words "owned automobile" to include any vehicle for which a title had

been requested but not received. Again, it did not do so.

Certainly appellant must have known that "owned" and "non-owned" would be construed in light of state statutes governing motor vehicles, especially when its own definition of "non-owned" simply was "an automobile or trailer not owned by the named insured, etc." Failure of an insurance company to define the words "owner" and "owned by" in a liability policy has been held by the Montana Supreme Court to create an ambiguity which was required to be resolved in favor of the insured and against the insurance company. *Keating v. Universal Underwriters*, (1958) 133 Mont. 89, 320 P.2d 351.

Therein, the Court said:

"... the first problem here posed, . . . is, whether or not the car was the 'property of others' or 'owned (by) the named insured' within the meaning of those phrases as employed in the insurance policy.

"It has been held that the term 'owner,' when used alone, imports an absolute owner or one who has complete dominion over the property owned as the owner in fee of real property, *Ramsey v. Leeper*, 168 Okla. 43, 31 Pac. (2d) 852, 859, and that the words 'owned by' mean an absolute and unqualified title, *Baltimore Dry Docks & Ship Building Co. v. New York & P.R.S.S. Co.*, 4th Cir., 262 F. 485, 488. Whether such is the meaning of the phrases here in question, or if the meaning is varied according to the connection in which they are used, and they are to be understood according to the subject

matter to which they relate, *McFeters v. Pierson*, 15 Colo. 201, 24 Pac. 1076, 22 Am.St.Rep. 388, it is certain, from the defendant's viewpoint alone, the phrases are at best generic and general and not specific and hence ambiguous and uncertain. The phrases are not defined in the insurance policy, nor is there any phraseology or conditions therein, nor is there anything in the facts submitted to this court from which may be inferred any qualified meaning, and, standing alone, we cannot say that these phrases were intended to exclude from the insurance coverage property possessed for sale only and to which the legal title resides in another, even though it be for security purposes alone.

"... If the defendant insurer had intended to exclude 'floored' automobiles from coverage, it would have been a simple matter for the insurer to have clearly and unequivocally provided therefor by the simple expedient of specifically referring to trust receipts and floor plans in the exclusion clause thereby removing all doubt. The law is plain that the ambiguity and uncertainty caused by the phrases in question must be resolved in favor of the plaintiff insured and against the defendant insurer. *Johnson v. Continental Casualty Co.*, 127 Mont. 281, 263 Pac. (2d) 551."⁽²⁾

ARGUMENT ON APPELLANT'S SPECIFICATIONS OF ERROR

All of appellant's specifications of error are argued as one, and we will do likewise. Essentially, of course, this appeal is from the trial court's denial of appellant's motion for summary judgment, and all present argu-

(2) Sec. 53-109 was not involved in the Keating case because of subsection (c) of 53-109. Subsection quoted on page 48 of appellant's brief.

ments, except one, were made to the trial court prior to the ruling set forth in the "Memorandum Opinion," filed April 1, 1964, (Tr., Vol. I. p. 37, et seq). The one point (relating to the effect of subsection (e)) which was not ruled on then was made by appellant's motion on December 21, 1964, (Tr., Vol. II, p. 4) and rejected by the trial court (Discussion, Tr., Vol. I, p. 62, et seq).

In its "Argument of the Case" (Br., p. 12 et seq), appellant first re-asserts the arguments raised in its December 21, 1964, motion, relative to *Sec. 53-109(e)*, *R.C.M. 1947*. Appellant contends, in essence, that title to the Ford could have been transferred by Mrs. Robert McCormick, as sole heir and administratrix of the estate of C. W. Ehart, to Albert Kinney solely by use of the procedures provided in *Sec. 53-109(e)*. This being so, it is contended, *Sec. 53-109(d)* is not applicable because *Sec. 53-109(d)* is said to apply only to applications for "titles" made under *Sections 53-109(a)* and *53-109(b)*, and not to applications made under *Sec. 53-109(e)*. (Br., top of p. 13.)

*APPELLEE'S ARGUMENT AS TO
EFFECT OF SECTION 53-109(e)
SUMMARY:*

APPELLEE CONTENDS, WITH RESPECT TO THE ABOVE, THAT TITLE COULD NOT HAVE BEEN TRANSFERRED FROM THE ESTATE OF C. W. EHART TO ALBERT KINNEY

SOLELY BY RECOURSE TO *SEC. 53-109(e)*,
EVEN IF SUCH HAD BEEN ATTEMPTED.

Our argument is quite basic, simply that *subsection (e)*, in its first 10 words, restricts its application to transfers by operation of law and the attempted transfer *from Mrs. McCormick to Albert Kinney* was not one by operation of law. Thus, *subsection (e)* is not applicable. Instead, the attempted transfer was a voluntary one, governed by *subsections (a), (b) and (d)*. The trial court adopted this position as the applicable Montana law. (Discussion, Tr., Vol. I, top of p. 64.)

Appellant seeks to avoid this seemingly obvious result by arguing that the Ford was paid for (Br., top of p. 15); that Albert Kinney had the use and possession of the Ford, purchased license plates for it, insured it and took no steps to rescind his contract to purchase it (Br., middle of p. 15). (In short, by asserting that some sort of equitable or qualified claim is tantamount to ownership under the law and the policies.) But appellant ignores the explicit statement of the Montana Supreme Court, in *Safeco Ins. Co. vs. Northwestern Mutual Insurance Co.*, (1963) 142 Mont. 155, 382 P.2d 174, that

“ . . . the provisions of the motor vehicle code provide the exclusive method of accomplishing a valid sale and transfer of a motor vehicle,”

(382 P.2d, at p. 179)

Appellant seeks next to avoid *subsection (d)* by

arguing (Br., p's 22 through the middle of p. 29) that the entire transfer from the estate of C. W. Ehart to Albert Kinney could have been (or was required to have been) completed solely under *subsection (e)*. It is asserted (Br., p. 25) that Albert Kinney, as the "successor in interest" of C. W. Ehart, could make application for a new title. We emphatically disagree, and an examination of *subsection (e)*, we submit, will exhibit the error in appellant's argument. The words "or successor in interest" emphasized by appellant (Br., p's 24 & 25) obviously are used in the statute to further extend, without specifically naming them, all of the possible entities through which the original owner's title passes by operation of law. For example, guardians, referees in bankruptcy, special administrators and probably many others. But these entities (and those named in the statute) are representing the original owner of legal title. The statute does not say that the recipient of the interest transferred by operation of law, (i.e., the legatee, heir, creditor, beneficiary, purchaser at sheriff's sale, or other persons acquiring title through the executor, administrator, receiver, trustee, sheriff or other representative or successor in interest) could forward an application for registration. Moreover, the phrase "successor in interest" certainly cannot be stretched, as appellant suggests, to cover a subsequent purchaser, as was Albert Kinney.

from a legatee, creditor, heir, beneficiary, or purchaser at sheriff's sale, for this would be a voluntary transfer. Therefore, we contend Albert Kinney alone could not have applied for a title in the manner stated.

As we have stated heretofore in this brief, what the parties should have done to accomplish the intended result was for the administratrix (Mrs. McCormick) to forward to the Registrar of Motor Vehicles an application for registration on the usual form, together with a verified or certified statement of the transfer, setting forth the facts as set forth by appellant (Br., p. 25), to-wit:

"(1) the reason for involuntary transfer; (2) the title transferred; (3) the names of the persons to whom the title is to be transferred; (4) the process of procedure effecting such transfer; (5) such instruments as may otherwise be required by law to effect a transfer of title. . . ."

This would have resulted in a new certificate of ownership (title) being issued to Mrs. McCormick. Then she should have signed and acknowledged the certificate, as provided by *subsection (a)*, and delivered it to Albert Kinney for transmittal to the Registrar as required by *subsection (b)*. Failing in this, there was no effective transfer of ownership for any purpose because of *subsection (d)*.

In its brief, appellant emphasizes Nos. 3 and 4 (above quoted) and apparently contends that since the

applicant (here, Mrs. McCormick, as administratrix) could have inserted the names of the person to whom title was to be transferred and the "process of procedure" effecting such transfer, she could have put in any name she liked, including a subsequent purchaser from her, Albert Kinney. Again, we argue that this plainly is not authorized by the statute because any such succeeding transfer was a voluntary transfer and to attempt to proceed solely under *subsection (e)*, without complying with *subsections (a) and (b)*, would violate the express provisos of *subsection (e)* to the effect that its provisions would not apply to transfers "by voluntary act of the person whose title or interest is so transferred," and that the application for transfer must show the reason for the "involuntary transfer." We ask how Mrs. McCormick could have listed an "involuntary" reason for selling the Ford car to Albert Kinney.

The point appellant misses is that here we have three separate and distinct transactions, one a transfer by operation of law from C. W. Ehart to Robert McCormick, next a transfer by operation of law from Robert McCormick, (Perhaps the first two transfers could have been completed as one), and third, an attempted voluntary transfer from Mrs. Robert McCormick to Albert Kinney.

Appellant asserts (Br., p. 26) that the District

Court "completely missed" the point it was trying to make with regard to the above. We believe it more accurate to say that the District Court was cognizant of the point and ruled against it. (Discussion, Tr., Vol. I, p's 63, 64.)

On page 28 to the top of page 29 of appellant's brief, it is argued that because somebody had to own the Ford, and further because Mrs. McCormick "transferred her title to Albert Kinney, it is obvious that in order to get the title transferred the provisions of subsection (e) of §53-109 will have to prevail." We disagree with this contention for the following reasons:

First, Mrs. McCormick did not transfer her title to Albert Kinney, she only attempted to transfer her title to Albert Kinney, but the attempted transfer has been barred by *subsection (d) of Sec. 53-109, R.C.M. 1947*.

Second, it isn't only *subsection (e)* which will have to prevail in order to transfer title from Mrs. McCormick to Albert Kinney; as we have stated in answer to appellant's previous arguments, *subsection (e)* cannot be applicable to the transfer from Mrs. McCormick to Albert Kinney because it is a "voluntary" transfer, expressly not covered by *subsection (e)*.

Nowhere in its brief does appellant explain how the transaction between Mrs. McCormick and Albert Kinney differs from the "ordinary transfer" referred to on top of page 29 of its brief.

The historical portions of appellant's brief from the middle of page 29 to the bottom of page 33 would be relevant only in the event the transaction between Mrs. McCormick and Albert Kinney was not an ordinary, voluntary transfer governed by *subsection (d)*. In view of the trial court's decision that the transaction was ordinary and voluntary, it would not appear appropriate to argue the irrelevant matter.

It is also irrelevant, we submit, whether appellant's statement at the bottom of page 33 of its brief, as follows:

"At the time of the transaction between Albert Kinney and Mrs. McCormick, she was a 'successor in interest' to the title which had transferred by operation of law, first to Robert McCormick, and then after his death to her. Therefore the correct procedure for her was outlined in subsection (e) of the statute and the punitive effect of subsection (d) does not apply."

is an accurate statement of the law. It is probable that the "correct procedure *for her* (Mrs. McCormick) was outlined in subsection (e) of the statute" (underlining ours), and it may even be that *subsection (d)* didn't apply to the transfer by operation of law to her (the Montana Supreme Court has not ruled on that question), but that certainly does not mean the subsequent transfer from Mrs. McCormick to Albert Kinney was not covered by *subsection (e)*.

Appellant argues (Br. p. 34) that because Mrs. McCormick was not an "owner in or to a motor vehicle,

etc.," and thus could not transfer title to Albert Kinney under *subsection (a)* of *Sec. 53-109, R.C.M. 1947*, the trial court's designation of the transfer from Mrs. McCormick to Albert Kinney as a "voluntary" transfer asked for something that was "presently unworkable." As to the "presently" part, we must agree, and the trial judge pointed this out when he said:

"Obviously, the administrator of the estate and Mrs. McCormick should have taken proper steps under *subsection (e)* to obtain a certificate of ownership."

(*Discussion, Tr., Vol. I, p. 64.*)

After taking such steps, and upon receipt of the new certificate of ownership (title), Mrs. McCormick should have complied with *subsection (a)*. We see nothing in the statute which guarantees to anyone that a transfer from a deceased owner to a purchaser from an heir can be accomplished in one fell swoop.

Appellant says the lower court's reasoning to the effect that the transfer to Albert Kinney was required to have been in two steps, from Ehart to Mrs. McCormick and from Mrs. McCormick to Albert Kinney, is "an absurdity" (Br., p. 36) and that the lower court's ruling embodying this reasoning is an "incredible decision" (Br., p. 4). We submit that the lower court's decision not only is not incredible or absurd, it is well-reasoned and accurately reflects the intent of *Sec. 53-109*.

In a nutshell, appellant's position seems to be that

after an owner's death, and until a new certificate of ownership (title) is finally issued to someone, the heirs, legatees and possibly purchasers of such persons can transfer ownership of a motor vehicle willy-nilly without in any way complying with *subsections (a) and (b), Sec. 53-109*. We contend that it would be a perversion of the entire statute if its mandatory provisions could be dispensed with solely because the title owner died.

At the bottom of page 36 and top of page 37 of appellant's brief, it is said that the District Court's final ruling on this matter is at variance with the prior ruling on motion for summary judgment. The footnote quoted on page 37 of appellant's brief is cited as evidence. The footnote, however, does not say that there could be a direct transfer from the Ehart estate to Kinney, it merely says that in view of *subsection (e)* there was a method whereby Mrs. McCormick could procure a title certificate and then endorse it over to Albert Kinney. The later opinion by Judge Jameson is, of course, the best indication of what he meant by the footnote.

ARGUMENT AS TO EFFECT OF SEC. 53-109(d)
(VOIDABLE VS. VOID CONTRACT)
SUMMARY:

APPELLEE'S CONTENTION IN THIS REGARD
MERELY IS THAT NOMENCLATURE OF THE
CONTRACT BETWEEN MRS. McCORMICK

AND ALBERT KINNEY AS VOIDABLE OR VOID MEANS NOTHING — THE PURCHASE CONTRACT BETWEEN MRS. McCORMICK AND ALBERT KINNEY WAS INVALID AND INEFFECTIVE FOR ANY PURPOSE BECAUSE THE STATUTE (*SEC. 53-109(d)*) MADE IT SO.

Appellant asserts that the purchase contract between Mrs. McCormick and Albert Kinney was not void but voidable (Br., p. 37); that Albert Kinney never acted to rescind it (Br., p. 38) and that until rescinded it is valid and binding without regard to *subsection (d)*, (Br., p. 41). Appellant raised this point before the trial court and it was disposed of by Judge Jameson in his opinion denying appellant's motion for summary judgment (Memorandum Opinion, Tr., Vol. I, p. 43).

We do not see that it is essential, or even desirable, to categorize the legal state of the sale and purchase contract on the date of the accident; patently the contract was not complete because *Sec. 53-109(d)* said it was not, and labeling the contract as voidable does not make it complete. We submit that until the contract was complete, Albert Kinney could not be considered the "owner" of the Ford.

Sec. 53-109 is a special statute on a special subject, and where in conflict with another statute, such as those cited by appellant (Br., p's 26 to 30), the special statute

must prevail. *Williamson v. Skerritt* (1963), 141 Mont. 422, 378 P.2d 215, at 218. To interpolate other statutes or to classify with textbook labels merely confuses the entire subject.

Sec. 53-109(d), in the simplest yet most obvious terms possible, says that if the registrar has not issued a certificate of ownership (title), three things occur: (1) delivery of the vehicle shall be deemed not to have been made; (2) title shall not have passed, and (3) the transfer shall be incomplete and not valid or effective for any purpose. This statute needs no construction. How appellant can take this subsection and argue that an unrescinded contract for purchase and sale of a motor vehicle, where no certificate of ownership has ever been requested, is not within its terms, is inconceivable. To hold so would be to hold that purchasers and sellers could virtually ignore the statutes requiring registration of motor vehicles just by refraining from rescinding their purchase and sales contracts. This flies directly in the face of the statement by the Montana Supreme Court in *Safeco*, *supra*, that

“... the provisions of the motor vehicle code provide the exclusive method of accomplishing a valid sale and transfer of a motor vehicle.”

(382 P.2d, at p. 179.)

We contend that no matter what rights Kinney had in the Ford, he wasn't the “owner” under the policies.

He wasn't the owner because both the statute and *Safeco*, supra, (which also dealt with "non-owned" vehicle coverage — see 382 P.2d, at 175), say he wasn't, and no semantic legerdemain can make him the owner. Judge Jameson felt the *Safeco* decision was controlling in this regard. (Discussion, Tr., Vol. I, p. 78.)

Parke v. Franciscus (1924), 194 Cal. 284, 228 Pac. 435, and the other cases cited by appellant (Br., p's 39, 40) are not applicable here. Most of such cases deal essentially with possessory claims or liens less than title or ownership.⁽³⁾

In *Parke v. Franciscus*, supra, the court held first that compliance with the registration statutes of California was essential to transfer of title (228 Pac., at 440, 441); secondly, it discussed the possessory rights of the parties. The Supreme Court of California has recently confirmed the holding in *Parke v. Franciscus*, supra, to the effect that compliance with the registration statute is

(3) *Dennis v. Bank of America, etc.*, (1939) 34 Cal.App.2d 618, 94 P.2d 51, and *Carpenter v. Devitt*, (1942) 49 Cal.App.2d 473, 122 P.2d 79, can be distinguished on another ground also, it being that the statute was different from Sec. 53-109. The California statute was amended, prior to the time the above cases were decided, to delete certain of the provisions of our statute and to add the defense of estoppel. See statute quoted, 122 P.2d, at p. 80 and 94 P.2d, at 53. In *Willard H. George, Ltd., v. Barnett*, (1944) 65 Cal.App.2d 828, 150 P.2d 591, the court held the section quoted in the above cases (Sec. 186) not even applicable to the facts. (150 P.2d, at 592). *Henry v. General Forming, Ltd.*, (1948) 33 Cal.2d 223, 200 P.2d 785, involved the same section (Sec. 186) after it had again been changed to delete some of the restrictive provisions (compare statute quoted, 200 P.2d 786 with 122 P.2d, at p. 80). See also, *Smith v. Western Casualty & Surety Co.*, (1943) 60 Cal.App.2d 508, 141 P.2d 10 for a tabulation of the statutory changes.

essential to transfer of title. (*Cooke v. Tsipouroglou* (1963) 31 Cal.Rep. 60, 381 P.2d 940, at 943.

The inapplicability of the cases dealing with title as distinguished from possessory claims, etc., is discussed in *U.S.F.&G. Corp. v. Myers Motors* (D.C.Va. 1956), 143 F.Supp. 96, at p. 99, as follows:

"* * * We believe that a clear distinction can properly be made between sales of motor vehicles, when title (or ownership or general property) is supposed to pass between the parties to the transaction, and other claims or liens less than title or ownership. It might well be that these recordation provisions are mandatory as to sales of motor vehicles in that they are designed for three very definite purposes: (1) To suppress automobile thefts; (2) to provide the state with a convenient and accessible record of title for tax purposes; (3) to provide a convenient and accessible method of identifying the ownership of an automobile for police purposes in connection with its operation on the highways of the state. These three reasons for attaching hard, deterrent results to any failure to comply with recordation statutes in connection with automobiles, do not exist as to liens or other claims less than title. Normally, one who has beneficial title to an automobile would be the one who would operate it on the highway, would pay the taxes and would be most concerned in preventing a theft of the car. The criminal sanctions under the Virginia Motor Vehicle Act, we think, were enacted primarily with reference to those having complete ownership, or at least beneficial title, as distinguished from security title or any lesser measure of interest in the automobile."

The point is also discussed in *Sly v. American Indemnity Co. of Galveston, Texas* (1932), 127 Cal.App.

202, 15 P.2d 522, wherein the insurance company's claim was quite similar to appellant's in this case. The Court said:

"From the above resume of the testimony of this witness it appears that there was some evidence that the insured had not, prior to the date of the accident, made a transfer of his interest in the automobile, and that, therefore, the court's finding that the insured had not sold and delivered the automobile to Mills is not entirely lacking in evidentiary support. This statement is made without taking into consideration the effect of noncompliance with the provisions of section 45, subdivision (c) of the California Vehicle Act (as amended by St. 1929, p. 514). The language of this section is as follows: 'Until said division shall have issued said new certificate of registration and certificate of ownership as hereinbefore in subdivision (d) provided, delivery of such vehicle shall be deemed not to have been made and title thereto shall be deemed not to have passed and said intended transfer shall be deemed to be incomplete and not to be valid or effective for any purpose.'

"This section appears to furnish an additional reason for sustaining the court's finding that no transfer of interest took place since it is undisputed that no new certificate of registration was applied for or issued prior to the date of the accident, and, therefore, under the plain language of the section, the intended transfer must be deemed to be incomplete and not valid or effective for any purpose. Appellant contends, however, that the exchange actually took place, possession of the automobile was surrendered to Mills, Krause not only took possession of the motorcycle but dealt with it as his own, and with the full consent and permission of Mills turned it over to the motorcycle dealer as the initial pay-

ment on the purchase price of another motorcycle. It is then argued by appellant that, although the hereinabove quoted section of the California Vehicle Act rendered transfer of the legal title impossible by reason of noncompliance therewith, nevertheless, transfer of an equitable interest was consummated and Mills became the equitable owner of whatever interest Krause, the insured, had in the insured automobile. To sustain the argument thus advanced, appellant cites a number of decisions wherein purchasers of motor vehicles in possession of such vehicles have been permitted to recover in actions of conversion or claim and delivery although such purchasers had not complied with statutory provisions requiring reregistration and the issuance of a new certificate of registration. It is to be observed that the decisions thus relied upon are cases wherein possessory actions were instituted by persons rightfully in possession and entitled to possession. Nevertheless, it must be conceded that their effect is to modify appreciably the very broad and plain language, hereinabove quoted, of section 45 of the California Vehicle Act."

Regardless of the above, however, we contend that cases from California and other states are not germane here. The Montana Supreme Court in *Safeco*, supra, has ruled on the effect of non-compliance with our registration statutes and has said, with regard to applicability of laws and decisions of other states:

"... we are duty bound to construe and judicially determine the provisions of the motor vehicle code as they are written, avoiding the multiple and confusing decisions of our sister states, because none of them contain the exact language present in our statutes."

(382 P.2d, at p. 178.)

Illustrative of the diversity of the decisions in other states are the many cases cited in *Blashfield, Cyclopedia of Automobile Law and Practice, Vol. I, Part I, Permanent Edition, sec. 304*, especially in the pocket part under footnote number 8.5, and *Vol. 7, Permanent Edition, Sec. 4252*.

Appellant (Br., p. 41, et seq) seeks to find some solace in *Firemen's Insurance Company of Newark, New Jersey v. Show, (D.C. Mont. 1953), 110 F.Supp. 523*. This case was cited to the court in *Safeco* and to the trial court. (Memorandum opinion Tr., Vol. I, p. 42.) However, the *Show* case was not in point in *Safeco* and is not in point here. The reason is that in *Show*, the prior owner's (Perry Motors) title certificate was executed in accordance with *Sec. 53-109(a)* and delivered to J. W. Show (the father of Jerry Show) on December 5, 1950. The certificate was duly transmitted to the Registrar of Motor Vehicles and on December 21, 1950, a new title was issued to J. W. Show (*110 F. Supp., at 525*). The accident happened in between, on December 17, 1950, at a time when the only insurance policy on the pickup was held in the name of Jerry Show, who actually paid for the truck. Judge Pray correctly held, on the title question, that the claim of the insurance company that title was still in Perry Motors because no certificate had issued on December 17, 1950, to J. W. Show,

was without merit. (*110 F.Supp. at 528, 529*). This is consistent with *Safeco* because *Safeco* held:

“it seems to us rather clear that when the seller has executed the transfer upon the certificate of ownership and delivered it and the motor vehicle the sale is complete and any delay on the part of the registrar in issuing the new certificate of ownership would have no effect. In any regular transaction the new certificate of ownership is required to be issued by the registrar and issues as a matter of course. The transfer then becomes complete and valid and dates back to the time of the transfer between the parties. If the transfer has not been made in compliance with the statute and the registrar by reason thereof does not issue a new certificate of ownership, clearly there was no transfer of ownership in its inception.”

(*382 P.2d, at 178.*)

The remainder of *Show* is merely a holding that since Jerry Show told the insurance company's agent of the title situation, before the policy was issued, the company waived the right to deny coverage on the ground that the insured's interest was other than unconditional and as sole owner, (*110 F.Supp, at 527*). This, also, is not alarming and would probably have ruled in the instant case if Albert Kinney had had an accident when the Ford policy was in existence. However, *Show* is not authority for any point involved in this litigation, nor, we submit, was it authority in *Safeco*.

At page 45 of appellant's brief appears the following:

"Thus far the Montana Court has not passed upon the question of ownership under an unrescinded contract for purchase of an automobile. . . ."

We question the correctness of this statement, even though the ultimate answer is not important to the issues on this appeal. In our view, *Safeco* involved a contract for purchase and sale of a motor vehicle which, at the time the accident occurred, as in the instant case, had not been rescinded. Liability under the policies involved in both the *Safeco* case and this case is determinable as of the date of the accident. The only way the result in *Safeco* could have been changed in this regard was for the parties to have executed and transmitted the certificate of ownership to the Registrar of Motor Vehicles within 10 days after the sale and upon issuance of a new certificate to Dean, his title would have reverted back to May 9, 1960, and he would have been considered the "owner" of the auto on May 11, 1960, the day of the accident. Since this was not done, the Court held no title passed to Dean. The ultimate rescission by Dean (if there was one) was quite irrelevant.

In the same paragraph (Br., p. 45) appellant contends that the Montana Supreme Court "has not passed upon the bearing of the definition of 'owner' found in *Sec. 59-133, R.C.M. 1947.*" (sic) This is not an accurate statement. In *Safeco*, (382 P.2d, at 179), the Court considered *Sec. 53-133* and held its definition of "owner"

would not govern where the context of *Sec. 53-109* required a different interpretation.

CONCLUSION

We respectfully submit that the judgment of the trial court is well founded, that all conclusions are reasonable and not clearly erroneous, and that the judgment should stand.

Respectfully submitted,

CROWLEY, KILBOURNE, HAUGHEY,
HANSON & GALLAGHER

By
Louis R. Moore
George C. Dalthorp
Attorneys for Appellee

I certify that, in connection with the preparation of this brief, I have examined Rules 18 and 19 of the United States Court of Appeals for the Ninth Circuit, and that in my opinion, the foregoing brief is in full compliance with those rules.

LOUIS R. MOORE
One of the Attorneys for Appellee

ACKNOWLEDGMENT OF SERVICE

Service of the foregoing Appellee's Brief and receipt of a true and correct copy thereof is hereby acknowledged this 15th day of February, 1966.

WIGGENHORN, HUTTON,
SCHILTZ & SHEEHY

By
Attorneys for Appellant

FEB 14 1967

No. 20550

**United States
Court of Appeals
for the Ninth Circuit**

NATIONAL FARMERS UNION PROPERTY
and CASUALTY COMPANY,

Appellant,

vs.

LAURENCE COLBRESE, JR.,

Appellee.

On Appeal from the United States District Court
for the District of Montana.

Appellant's Reply Brief

WIGGENHORN, HUTTON,
SCHILTZ & SHEEHY
403 Electric Building
Billings, Montana
Attorneys for Appellant

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LAURENCE COLBRESE, JR.,

Appellee.

On Appeal from the United States District Court
for the District of Montana.

Appellant's Reply Brief

Appellant National Farmers Union Property and Casualty Company respectfully replies to the brief interposed herein by the Appellee, as follows:

STATEMENT OF THE CASE

We find on page 2 of Appellee's brief the statement that "the brief of the appellant does not in some respects present accurately and fairly the evidence as it actually exists in the record." We find no further statement in Appellee's brief as to what particular statement made by appellant is unfair or inaccurate. Our examination of appellee's statement of facts does not appear to us to add anything of substance to the statement which appellant provided in its first brief. It does appear that appellee hopes to ameliorate the exclusive possession enjoyed by him of the 1949 automobile and the circumstances under which he enjoyed that exclusive possession. We want to emphasize therefore that the following admissions of fact were admitted by appellee as far back as January 22, 1964, (Tr., Vol. I, p. 19) and that they fairly and accurately represent the record in the case:

"5. From and since September 2, 1958, said Albert Kinney claims to be the sole owner, and thought himself to be the sole owner of all right, title and interest in and to the said 1949 Ford automobile.

"6. From and since September 2, 1958, said Mrs. Robert McCormick claims no right, title or interest in and to said automobile, and no other person than

said Albert Kinney claimed any right, title or interest in said automobile.

* * *

"8. Said Mrs. Robert McCormick, from and since September 2, 1958, thought that Albert Kinney was the owner of all right, title and interest in and to said 1949 Ford.

* * *

"11. Said Albert Kinney was under the impression that when the estate was finally settled he would get the title certificate issued by the registrar of motor vehicles to the car, with his name endorsed upon it as the certified owner; but that said Albert Kinney "figured the car was" his (p. 17, Kinney deposition).

"12. Said 1949 Ford has been in the possession of Albert Kinney from and since September 2, 1958, and under and subject to his direction and control."

(Tr., Vol. 1, pp. 16, 17)

*THE CONTRACT BY KINNEY TO PURCHASE
THE FORD WAS NOT VOID, BUT VOIDABLE:*

Appellee has not met this contention in his brief.

In the situation of the purchase of the Ford, as it exists between the seller and Albert Kinney, the latter had possession of the Ford under a contract of purchase, but voidable by him. He did not act to void it. In fact, "from and since September 2, 1958, Albert Kinney claimed to be the sole owner, and thought himself to be the sole owner" of the 1949 Ford automobile (Admissions, Tr., Vol. I, p. 16).

Under *Grady v. Livingston* (Mont. 1943) 115 Mont. 47, 56; 141 P.2d 346, 350, the rights of parties under a voidable contract may not be disregarded until they have been declared void by a court having jurisdiction. Moreover the parties may elect to proceed under a voidable contract.

The Montana cases of *Safeco*, *Sonnek* and *Firemen's Insurance Company of Newark v. Shaw* are not otherwise explainable except one recognizes the distinction between a void and a voidable contract. In *Sonnek* (*Sonnek v. Universal C.I.T. Credit Corp.*, 374 P.2d 105, 140 Mont. 503) the purchaser had taken direct action to rescind the contract of purchase. In *Sonnek*, the Montana Court held in effect that when the seller failed to transfer the title there was a failure of consideration and such failure of consideration was a basis for the rescission.

In *Safeco* (*Safeco Insurance Company of America v. Northwestern Mutual Insurance Company*, 382 P.2d 174, 142 Mont. 155) it is particularly important that the facts do reveal a rescission of the contract by the parties, and a return to the *status quo*. There had been a rescission of the contract, if a contract in fact existed between the parties in *Safeco*. Appellee, in his brief, (page 34) disputes our point here only to the effect that no rescission had occurred on the date of the accident. This,

however, would not affect the status of the parties because even under the holding of Safeco, even after the accident, if the certificate of ownership had been issued, "the transfer then becomes complete and valid and dates back to the time of the transfer between the parties." (382 P.2d, 178) In a void contract it would not be possible for the title to relate back or the transfer to be complete as of the date of the transfer between the parties. So the contract was voidable.

The decision in the *Firemen's Insurance Company* case (*Firemen's Insurance Company of Newark, New Jersey v. Show*, 110 F. Supp. 523 (U.S.D.C., Mont.)) presents a different facet of the problem. Appellee apparently agrees that the holding by Judge Pray in this case was correct (p. 32, Appellee's Brief) and indeed so does appellant. The appellee, however, in believing that Judge Pray was correct in the *Firemen's Insurance Company* case is not consistent. If Judge Pray had applied the strict meaning of Sec. 53-109 (d), as appellee is contending for here, then he would have held that since the paper title had not transferred to Show the transfer was incomplete and not valid for any purpose. In effect Judge Pray, rightfully as all parties agree, held against the strict terms of the statute. One finds no difficulty in the Pray decision, however, if one realizes that in the *Firemen's Insurance Company* case *the*

purchaser of the automobile had not taken action to rescind the contract. In fact he had taken steps to complete the contract.

In that respect the *Firemen's Insurance Company* case is similar to the case at bar. Here *Albert Kinney has not taken any steps to rescind the contract.* In fact, he "claims to be the owner of the automobile since September 2, 1958," and he has done what he could to complete the contract, including making demands for transfer of the title to him.

As between the seller and Albert Kinney therefore there is in existence a valid, though voidable, contract of purchase.

When the Montana Court, in *Safeco*, states that the title relates back and a transfer becomes complete and valid as of the time of transfer once a certificate of ownership has been issued, it in effect is taking into account the distinction between a void and a voidable contract. In this respect it is in agreement with the holding in *Park v. Franciscus* (1924) 194 Calif. 284, 228 Pac. 435, which stated that the failure of the transferee of the ownership in the car to procure the registration statement does not make the sale "void ab initio." (228 Pac. at page 439)

Incidentally, one receives the impression from appellee's brief that *Park v. Franciscus* is not applicable

here. We disagree. It is a holding, in a sister state, with respect to a provision of statute identical to the provisions in 53-109(d). Regardless of the fact that the State of California later modified its statute to soften the punitive effect of such provisions, the holding in *Park v. Francisco* is clear, rational and applicable to this case.

We therefore earnestly contend that unless one has in mind the distinction between a void and voidable contract, the decisions in *Safeco* and *Sonnek* by the Montana Supreme Court on the one hand, and a decision by Judge Pray in *Firemen's Insurance Company of Newark, New Jersey*, on the other hand, are incompatible. For if 53-109 (d) must be strictly construed without respect to the concept of voidable contracts, then Judge Pray was wrong in the *Firemen's Insurance Company* case.

A void contract does not need rescission; it cannot be validated by ratification or made to relate back (17 Am. Jur. 2d 342, 343). A voidable contract, on the other hand, is valid and binding until it is avoided by the party entitled to avoid it (17 Am. Jur. 2d 342, 343, Sec. 7, Contracts).

The situation between the seller and the purchaser of the automobile in this case, *even now*, is that the seller could deliver the certificate of title to the buyer, by whatever means obtained, and the transaction would become complete, and would relate back to the date of

transfer between the parties (*Safeco*, 382 P.2d, at 178).

***UNDER STRICT CONSTRUCTION OF 53-109(d)
POSSESSION OF THE FORD NEVER TRANS-
FERRED TO KINNEY.***

If the punitive effect of 53-109(d) with respect to the transfer of ownership is to be applied in this case, then there is another portion of that statute, equally punitive, that must also be taken into consideration.

The statute also provides that in the event of failure of transfer of the registration certificate, "delivery of any motor vehicle shall be deemed not to have been made * * *." (Sec. 53-109(d), R.C.M. 1947)

Thus under the strict terms of the statute, if title did not pass, *possession of the automobile did not pass either* and on the date of the fatal accident Jerry Kinney was was not driving the 1949 Ford. Therefore no insurance coverage would attach under this action.

***TITLE COULD BE TRANSFERRED TO KIN-
NEY UNDER 53-109(e); IN WHICH CASE 53-
109(d) WOULD NOT APPLY.***

Appellee reads restrictions into subsection (e) of 53-109 that are not found in its language. There is no restriction preventing the Registrar of Motor Vehicles in Montana from transferring the title to any person lawfully or legally entitled thereto, once the transfer has occurred by operation of law.

Plainly subsection (e) provides that the "successor

in interest" of the person whose title and interest is so transferred may procure a certificate of title.

In this case, the holder of the registered title is C. W. Ehart. He is dead and his estate is being probated; his only heir, Robert W. McCormick, is also dead and his sole heir is Mrs. Robert McCormick. She is not only the only heir and "successor in interest" to the title or ownership of the Ford, but she is also the administratrix of the Ehart estate. Thus she could act as administratrix in procuring the title. For this reason the District Court was correct when it stated in its footnote to its Memorandum Opinion (Tr., Vol. I, p. 40) that in view of this statutory provision there is no reason why the title certificate could not have been endorsed and delivered to Kinney "prior to the completion of the Ehart and McCormick estates." There is in fact no reason otherwise, and this procedure could have been followed *and could now be followed* to transfer the title to Albert Kinney. Once it is admitted that such procedure could occur under subsection (e), then the provisions of subsection (d) do not apply. Appellee does not argue this latter point, although he dismisses it as irrelevant. But nevertheless, both grammatically and historically, the punitive provisions of subsection (d) do not apply to procedures under subsection (e) of the statute.

Under the strict construction of subsection (e) as

contended for by Appellee, the title could not be transferred prior to the completion of the Ehart and McCormick estates. The Ehart estate, at least, would have to be completely probated so as to vest the title in the Robert McCormick estate. Then only, according to appellee's construction of the statute, could Mrs. McCormick get a title in her name, as the heir to the Robert McCormick estate. We have stated in our prior brief, and we state it again, that this contention is an absurdity, and such procedure is certainly unnecessary. There is no statutory reason why title could not be given directly to Kinney in the Ehart estate without waiting for the probate of the McCormick estate. Again, once it is admitted that this could be done under subsection (e) of the statute, then the punitive provisions of subsection (d) do not apply.

THE DEFINITION OF "OWNER" IN SEC. 53-133, R.C.M. 1947 IS APPLICABLE HERE, AND INCLUDES ALBERT KINNEY.

Sec. 53-133, R.C.M. 1947 contains a series of definitions that are to be applied to the motor vehicle registration act in its entirety. With respect to who is an "owner" the section on definitions provides as follows:

"53-133 (1763). *Definitions.* The words and phrases used in this act shall be construed as follows, unless the context may otherwise require:

* * *

f. The term 'owner' shall include any person, firm, association or corporation owning or renting a motor vehicle, or *having the exclusive use thereof*, under lease or otherwise, and *shall also include a contract vendee.*" (Emphasis supplied)

Taking the definition as it stands, Albert Kinney was the "owner" of the 1949 Ford. He had the exclusive use thereof, and had had that exclusive use more than two years. He claimed to own the vehicle and no other person makes any claim thereto. Moreover while he was awaiting the delivery to him of title he was a "contract vendee." Thus, under the statute, Albert Kinney was the "owner" of the automobile and as such the 1949 Ford was not a non-owned automobile under the provisions of appellant's insurance policy.

Appellee's brief (p. 34) contends that the Montana Court in *Safeco* has held that *Sec. 53-133* does not apply. However, that is not precisely what the court said. It made the following statement in *Safeco*:

"As to Sec. 53-133, R.C.M. 1947, a statute defining words and phrases in the motor vehicle code, it clearly states that their construction shall be 'unless the context may otherwise require.' If there exists any conflict, *which we do not perceive*, in our view the context of Sec. 53-109 requires the interpretation as herein stated." (Emphasis supplied)

(382 P.2d, at page 179)

It is clear from the foregoing statement that the Court did not perceive any conflict between the pro-

visions of *Sec. 53-133, R.C.M. 1947* and the facts as they appeared in the *Safeco* case.

It must be remembered that in *Safeco* we had the case of a rescinded contract, if there ever existed a contract between the parties. The exact statement in *Safeco* is that

“* * * Following Dean's recovery from his injuries either he or his wife took the Hillman car back from the sales lot at Bear Paw and the matter was at an end.”

(382 P.2d, at page 177)

Thus in *Safeco* we have a situation where it was not possible for the title to relate back to the day of transfer between the parties as is possible in this case. Moreover, there was no exclusive possession of the automobile continuing in the purported buyer in *Safeco*, and certainly he was not a “contract vendee” in the *Safeco* case.

Nothing in the context of *53-109* is in conflict with the context of *Sec. 53-133*, defining “owner,” when the facts show, as in this case, that there is an unrescinded contract for sale of the automobile. Even though the transfer is “incomplete” under the terms of *Sec. 53-109(d)*, nevertheless the purchaser in the incomplete contract has the exclusive possession of the automobile and is of course a contract vendee. Thus he is an owner within the terms of the definition in *Sec. 53-133*.

Moreover, if, as we contend here, the transfer could

be accomplished under the terms of subsection (e) of *Sec. 53-109, R.C.M. 1947*, then there is no conflict at all with the provisions of *Sec. 53-133*, because, as we have pointed out, if proceedings to transfer title occur under subsection (e) of the recording statute the punitive effect of subsection (d) does not apply.

The definition of "owner" therefore in *Sec. 53-133* is applicable and under it the 1949 Ford was not a "non-owned automobile" in this case. (*Yoshida v. Liberty Mutual Insurance Company*, 240 F.2d 824)

CONCLUSION

Wherefore, the appellant, having fully replied to the brief of the appellee herein, respectfully prays that this Circuit Court of Appeals reverse the judgment of the lower court and direct judgment in favor of the appellant.

Respectfully submitted this day of March, 1966.

WIGGENHORN, HUTTON,
SCHILTZ & SHEEHY

By JOHN C. SHEEHY
Attorneys for Appellant

CERTIFICATE

John C. Sheehy, an attorney duly authorized to practice in the United States Court of Appeals for the Ninth Circuit, states as follows:

I certify that, in connection with the preparation of this brief, I have examined Rules 18 and 19 of the United States Court of Appeals for the Ninth Circuit, and that in my opinion, the foregoing Brief is in full compliance with those rules.

JOHN C. SHEEHY
Attorney for Appellant

ACKNOWLEDGEMENT OF SERVICE

Due service of the within and foregoing Appellant's Reply Brief and receipt of 3 copies thereof, made and admitted this day of March, 1966.

CROWLEY, KILBOURNE, HAUGHEY,
HANSON & GALLAGHER

By LOUIS R. MOORE
Attorneys for Appellee

FEB 14 1967

No. 20550

United States Court of Appeals for the Ninth Circuit

NATIONAL FARMERS UNION PROPERTY
and CASUALTY COMPANY,

Appellant,

vs.

LAURENCE COLBRESE, JR.,

Appellee.

On Appeal from the United States District Court
for the District of Montana.

Petition for Rehearing

WIGGENHORN, HUTTON,
SCHILTZ & SHEEHY

403 Electric Building
Billings, Montana

Attorneys for Appellant

CROWLEY, KILBOURNE, HAUGHEY,
HANSON & GALLAGHER

500 Electric Building
P. O. Box 2529

Billings, Montana

Attorneys for Appellee

Filed _____, 1966

_____, Clerk

United States Court of Appeals for the Ninth Circuit

NATIONAL FARMERS UNION PROPERTY
and CASUALTY COMPANY,

Appellant,

vs.

LAURENCE COLBRESE, JR.,

Appellee.

On Appeal from the United States District Court
for the District of Montana.

Petition for Rehearing

To the Honorable Circuit Judges Barnes, Jertberg and
Ely of the United States Court of Appeals for the
Ninth Circuit:

Appellee requests a rehearing. This Court has held that it is the duty of the Federal Court to examine and ascertain how the local State Supreme Court would decide a case.

Young v. Aeroil Products Co., 1957,
9th C.C., 248 F. 2d 185.

This Court has held that the considered view of a district court as to the law of the state in which it sits will not be reversed unless shown to be clearly wrong, or inescapably wrong, or patently erroneous.

Bellon v. Heinzig, 1965, 9th C.C.,
347 F. 2d 4;

Gumataotao v. Government of Guam,
1963, 9th C.C., 322 F. 2d 580.

District Judge W. J. Jameson investigated to ascertain how the Montana Supreme Court would decide this case. He procured the briefs on appeal submitted to the Montana Supreme Court in *Safeco Ins. Co. of America vs. Northwestern Mutual Insurance Co.*, 1963, 142 Mont. 155, 382 P. 2d 174. The reasons upon which the present opinion of this Court is based were presented to and rejected by the Montana Supreme Court in *Safeco*. Respondent in *Safeco* in his brief urged:

"I.

"STATEMENT OF THE CASE

"A. SUMMARY

" * * *

"At the time of the accident Dean owned a liability insurance policy issued by Safeco, and Bear

Paw owned a liability insurance policy issued by Northwestern. If Dean was the 'owner' of the car on May 11th, the Safeco policy is responsible. If Bear Paw was the 'owner' on May 11th, Northwestern is responsible.

"The sole problem in the case is one of definition. What does the word 'owner' mean as used in two policies?" (*P. 5.*)

He cited and quoted the following Montana R.C.M. 1947 statutes—53-133(f); 53-419; 53-109. In argument he said:

"II.

"ARGUMENT

"A. *THE PROBLEM*

"The problem here is one of definition. What does the word 'owner' mean as used in the insurance policies written by the respective companies? An insurance policy is a contract. (Sec. 2, Ch. 286, L. 1959.) Contracts of insurance are to be interpreted as other contracts, and must be interpreted to give effect to the mutual intention of the parties. (Sec. 13-702, R.C.M. 1947; *Stevens v. Steck*, 101 Mont. 569, at 576, 55 Pac. 2d 7.)

"Respondents contend that Section 53-109(d) R.C.M. 1947, is a recording statute governing the record title as distinguished from ownership; that Section 53-133, R.C.M. 1947, defines ownership.

"Respondents recognize the rule that the law in existence at the time of the formation of a contract may be read into it. (Appellants' Brief, p. 35-36.) Such rule is of no real assistance here because the problem is, which law do we read in? The major effort of this brief is to indicate that Section 53-133 R.C.M. 1947, which defines 'owner' should be read into the contract, and that Section 53-109(d), which does not so much as use the word 'owner', should not.

"B. *THE MEANING OF THE WORD
'OWNER.'*

"(1) *The intention of the parties and practical consideration.*" (Pp. 13-14.)

* * *

"(2) *Dean was the Owner under the General Law of Sales.*" (P. 18.)

* * *

"(3) *The Statute of Frauds.*" (P. 20.)

* * *

"4. *The registration law (Section 53-109d) should not control the definition of ownership.*

"It is Respondents' position that the insurance policies involved should not be defined on the basis of Section 53-109d, because:

"(a) Such a result is unrealistic,

"(b) Is not compelled by the statutes,

"(c) Is not compelled by the case authority.

"(a) *A literal application of 53-109d is unrealistic.*" (P. 24.)

* * *

"5. *Section 153-133(f), R.C.M. 1947 should control the meaning of the word 'owner'.*" (P. 28.)

He discussed not only Montana case authority, but he expended 13 printed pages on the California registration law and California decisions. (Pp. 32-46.)

Is it not significant that the Montana Supreme Court rejected these same arguments and reasons upon which the present opinion is based?

If the present opinion is permitted to stand, it will not only reverse the considered view of the local District Court after investigation of local Montana law, it

will directly contradict or reverse the action previously taken by the Montana Supreme Court in *Safeco*.

The present opinion relies upon the interpretation of California law in *Yoshido*, and the Hawaii law in *Teixeira*. The effect of those cases is that the word "owned" means something less than an absolute and unqualified title. Not only did the Montana Supreme Court reject the viewpoint represented by these cases in *Safeco*, Montana has held directly to the contrary in *Keating v. Universal Underwriters*, 1958, 133 Mont. 89, 320 P.2d 351. That case holds that "owned by" means an absolute and unqualified title, and that failure of an insurance policy to define "owned" creates an ambiguity which must be resolved against the insurance company.

Appellee did not argue orally or in brief the reasons upon which the present opinion is based. They were rejected by the Montana Supreme Court in *Safeco*; that fact had been investigated and ascertained by District Judge Jameson; and appellee believes that before the considered view of the District Judge is reversed, that appellee should be permitted on rehearing to show how the Montana Supreme Court has in fact already considered and rejected the same reasons.

Respectfully submitted,

CROWLEY, KILBOURNE, HAUGHEY,
HANSON & GALLAGHER

By: CALE CROWLEY

One of the Attorneys for Appellee

I certify that in connection with the preparation of this Petition For Rehearing, I have examined Rule 23, and, in my opinion, the foregoing is in full compliance, is well founded, and is not interposed for delay.

CALE CROWLEY

One of the Attorneys for Appellee

ACKNOWLEDGEMENT OF SERVICE

Service of the foregoing Petition and receipt of a true and correct copy thereof is hereby acknowledged this 29th day of November, 1966.

WIGGENHORN, HUTTON,
SCHILTZ & SHEEHY

By:.....
Attorneys for Appellant

FEB 11 1986

N O. 20551 /

IN THE UNITED STATES COURT OF APPEALS
FOR THE NINTH CIRCUIT

ROBERT DULAINÉ,

Plaintiff and Appellant,

vs.

UNITED STATES OF AMERICA,

Defendant and Respondent.

APPELLANT'S OPENING BRIEF

FILED

FEB 11 1986

WM. B. LUCK, CLERK

JAFFE, OSTERMAN & SOLL

By: F. FILMORE JAFFE

6380 Wilshire Boulevard

Suite 900

Los Angeles, California 90048

Attorneys for Appellant

N O. 2 0 5 5 1
IN THE UNITED STATES COURT OF APPEALS
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JAFFE, OSTERMAN & SOLL
By: F. FILMORE JAFFE
6380 Wilshire Boulevard
Suite 900
Los Angeles, California 90048

Attorneys for Appellant

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IN THE UNITED STATES COURT OF APPEALS
FOR THE NINTH CIRCUIT

ROBERT DULAINÉ,

Plaintiff and Appellant,

vs.

UNITED STATES OF AMERICA,

Defendant and Respondent.

APPELLANT'S OPENING BRIEF

I

STATEMENT OF THE CASE

On November 13, 1964, Appellant ROBERT DULAINÉ, filed a Complaint in the above captioned matter against the UNITED STATES OF AMERICA, under the Federal Tort Claims Act, 28 U.S.C. §1346(b), 2671-80, for damages resulting from negligence which is alleged to have occurred within two years of the filing of said Complaint (Clk. Tr. pp. 2-6, inclusive).

On July 16, 1965, Respondent UNITED STATES OF AMERICA, filed a Notice of Motion and a Motion for Summary Judgment, in accordance with the provisions of Rule 56(b) & (c)

of the Federal Rules of Civil Procedure, in that the pleadings and all of the documents filed in this action show that Respondent is entitled to a Judgment as a matter of law.

Respondent also moved in same Motion, in the alternative, that should the Court deny the Motion for Summary Judgment, for an Order, pursuant to Rule 42(b) of the Rules of Civil Procedure, directing that the issue as to whether or not Appellant's Complaint was timely filed, be separated and tried and disposed of at the Court's convenience.

In support of said Motion for Summary Judgment, MORTON H. BOREN, then an Assistant United States Attorney, caused to be filed his Affidavit (Clk. Tr. p. 22, lines 1 through p. 24, line 10), and a Memorandum of Points and Authorities (Clk. Tr. p. 10).

On August 18, 1965, Appellant caused to be filed his Affidavit in Opposition to Motion for Summary Judgment (Clk. Tr. p. 25, line 18 through p. 34, line 23).

On August 24, 1965, THE HONORABLE IRVING HILL, Judge of the United States District Court, made certain Findings of Fact and Conclusions of Law on Respondent's Motion for Summary Judgment (Clk. Tr. p. 36, et seq.), and based upon such Findings of Fact and Conclusions of Law, granted Respondent's Motion for Summary Judgment (Clk. Tr. p. 40).

It is to this Judgment of Dismissal that Appellant files this appeal.

II

THE AFFIDAVIT OF APPELLANT IN OPPOSITION TO RESPONDENT'S MOTION FOR SUMMARY JUDGMENT, WHEN CONSIDERED WITH THE PLEADINGS ON FILE, ESTABLISHES THAT THERE WAS ONE OR MORE ISSUES OF FACT TO BE DETERMINED BY THE TRIER OF FACT, SO THAT A MOTION FOR SUMMARY JUDGMENT SHOULD HAVE BEEN DENIED.

The Appellant is seeking recovery for damages that he alleges were sustained by him as a result of negligence on the part of the Veterans Administration personnel.

The Federal Tort Claims Act provides the time limit within which a tort action may be brought against the United States. This statute of limitations is found in 28 U.S.C. §2301 subd. (b) and reads as follows:

"(b) A tort claim against the United States shall be forever barred unless action is begun within two years after such claim accrues. . . ."

The Complaint alleges, among other things, that within two years last past (that is, within two years preceding November 13, 1964, the date the action was filed), Appellant discovered for the first time that during the period that Appellant was under the care of WILLIAM A. TAYLOR, L. NEWMAN and such other doctors, nurses, aides, laboratory technicians, residents, interns, externs and attendants, and each of them, said parties, and each of them, failed to exercise the skill, care and degree of learning ordinarily

possessed by physicians and surgeons, nurses, aides, laboratory technicians, residents, interns, externs and attendants practicing their respective professions in the same locality, and negligently, carelessly and unskillfully diagnosed, evaluated, cared for, treated, operated upon, nursed, managed, attended to and provided for Appellant so as to proximately cause grievous injuries to his body and extremities (Clk. Tr. p. 4, lines 19-31).

In support of Respondent's Motion for Summary Judgment, MORTON H. BOREN filed his Affidavit (Clk. Tr. p. 22), wherein he states,

"2. That he has reviewed the medical records of the Veterans Administration relating to the medical treatment rendered to the plaintiff.

"3. That the plaintiff's medical records contain the following facts:

"(a)

"(b)

"(c)"

Hearsay statements contained in an affidavit will not be considered in determining the motion. Dyer v. Mac Dougal, 201 F.2d 265.

In conformity with Rule 56, subd. (e), Appellant's Affidavit in Opposition to Motion for Summary Judgment (Clk. Tr. pp. 25 to 34) was made on personal knowledge and set forth facts that would be admissible in evidence, and showed affirmatively that Appellant

was competent to testify as to the matters therein stated. In said Affidavit, Appellant raised a material issue of fact when he stated under oath that he was not aware of the malpractice until he learned the true facts late in November, 1962.

Appellant stated in his Affidavit as follows (Clk. Tr. p. 25, lines 26-32 and on p. 26, lines 1-2):

"I did not know a rent had been cut in the main vein to the left leg soon after the operation in 1956. It was only after I learned the full facts of the operation for arteriovenous aneurysms that I realized that this was without a doubt a case of negligence and malpractice on the part of the Veterans Administration doctors. I learned the true facts late in November of 1962, when all of my hospital records were released from Sawtelle Veterans Hospital."

Again in Clk. Tr. p. 26, lines 9-22, the Appellant stated:

"I discovered the omission of facts in 1963 and 1964 when I received and reviewed my medical records that were sent to me by Louis Litwin, and compared my compensation rating with the Schedule for Rating Disabilities that was sent to me from Washington, D. C., by Mr. A. W. Farmer, Director, Compensation, Pension and Education Service of the Veterans Administration. This was sent to me on June 11, 1964. The Schedule for Rating Disabilities of the Federal Register is dated May 22, 1964, and

was not available before that date. Therefore, it would have been impossible for me to have the information that was needed for my claim before that date. It was classified until May 22, 1964, when Congress decided that Veterans should have more information on their disabilities and made this a public document."

Again in Clk. Tr. p. 27, lines 23-26, the Appellant states:

"Now, when I learned in 1963 for the first time, that the Veterans Administration Adjudication office did not have any 'foreign bodies' listed, I requested an x-ray examination."

Again in Clk. Tr. p. 30, lines 2-10, the Appellant states as follows:

"Reference is made to line 22 of page 4 of defendant's Memorandum: 'It was then necessary to ligate the left common iliac vein.' Query: 'Why did counsel fail to list that it was also necessary to ligate the "hypogastric vein, left external iliac vein and large gluteal branch of left common iliac vein".' Of course, I don't know how necessary it was, but this was done during the operation and was concealed from me until the release of my records in the latter part of November of 1962."

Again in discussing the matter of discovery of the malpractice, the Appellant in his Affidavit, Clk. Tr. p. 31, line 17 through

p. 32, line 2, states:

"Shortly after September 29, 1964, Plaintiff received from the VA, a 'Statement of the Case' as required by law.

"In the statement of the case, on page 7, listed after the date November 27, 1963, is the following sentence: 'Received application for compensation, Form 21-526A for Malpractice during A-V fistul operation at Sawtelle VA Hospital on September 26, 1956.' The fact that there is a form for Malpractice in a government hospital was concealed from me by the Veterans Administration until late in 1963, even though I brought this to their attention in 1962 when my records were released, and when I discovered that this was malpractice.

"The 'Statement of the Case' of September 29, 1964, on page 13 in the second paragraph lists the reasons for the decision not to award payment for malpractice. There is no mention of STATUTE OF LIMITATIONS. If the Statute of Limitations has expired in this case, it would have to be listed in the 'Statement of the Case'. It was not listed, and therefore, it does not apply."

In replying to the Respondent's Memorandum concerning the discovery of the negligence, Appellant stated in his Affidavit,

Clk. Tr. p. 32, line 20 to p. 33, line 1 and p. 33, lines 9-12, as follows:

"On page 9a of Defendant's Memorandum, starting with line 12, it states, 'Although in answer to Interrogatory No. 3, the plaintiff alleges that his treatment from February 14, 1956 to date has been negligent, it should be noted that no mention is made in his answer to Interrogatory No. 2 of any negligent acts or omissions subsequent to his operation in September, 1956.'

"In answer to this I would like to say:

"1. The failure of the doctor to inject the proper amount of dye is listed under (a) Improper technique in performing aortogram. This was not discovered until my records were released in November of 1962.

"2. The failure to diagnose aneurysms or fistulas was not corrected until November 26, 1963.

"

"The Veterans Administration doctors didn't admit the ligation of the common iliac vein, the external iliac vein, the hypogastric vein and the large gluteal branch of the iliac vein until 1963."

Again responding to Respondent's Memorandum, Appellant in his Affidavit, (Clk. Tr. p. 34, lines 5-10), stated:

"On page 10 of Defendant's Memorandum, counsel lists several letters. All of the letters were requesting compensation for disability. There was never any claim for malpractice for the simple reason that I did not know that there was malpractice until I received and reviewed my medical records in the latter part of November of 1962."

One who moves for summary judgment has the burden of demonstrating clearly that there is no genuine issue of fact. Any doubt as to the existence of such an issue is resolved against him. The evidence presented at the hearing is liberally construed in favor of the party opposing the motion and he is given the benefit of all favorable inferences which might reasonably be drawn from the evidence. Facts asserted by the party opposing the motion and supported by affidavits or other evidenciary material, must be taken as true. Janek v. Celebrezze, 336 F.2d 828; Kilfoyle v. Wright, 300 F.2d 626.

This is so even though the moving parties show that the responding party has made admissions that are inconsistent with statements in his affidavits. This situation, the courts say, do no more than raise an issue of fact, which makes a trial necessary. Eagle Oil & Refining Co. v. Prentice, 19 Cal.2d 553.

The very first sentence in Respondent's Memorandum of Points and Authorities (Clk. Tr. p. 10, lines 4-9) recites as follows:

"It is clear that if this action is tried on the issue of negligence or malpractice, it will take considerable court time due to the need for extensive medical expert testimony to determine the facts concerning the alleged negligence and malpractice on the part of the defendant's agents and employees in treating the plaintiff."

The granting or withholding summary judgment should never be based upon the factor of saving time or expense. Aileen Mills Company v. Ojay Mills, Inc., 188 F. Supp. 138.

The Appellate Courts have stated with monotonous regularity that the purpose of the summary judgment procedure is to provide a method for the prompt dispositions of actions where there is, in fact, no triable material issue. The Court's duty is limited to the determination of whether or not factual issues are presented by the affidavits, and it is no part of the Court's duty to make any factual determination. Miller v. Miller, 122 F.2d 209; Tobelman v. Missouri-Kansas Pipeline Company, 130 F.2d 1016; Stevens v. Howard D. Johnson Company, 181 F.2d 390; Union Transfer Company v. Riss and Company, 218 F.2d 553.

The procedure authorized by Rule 56(b) & (c) of the Federal Rules of Civil Procedure is, of course, a drastic one, requiring caution in its application and may not be used as a substitute for the traditional method of determining factual issues. Hoffman v. Babbitt Bros. Trading Company, 203 F.2d 636; United Meat

Company v. RFC Company, 174 F.2d 528; Busman Construction Company v. Conner, 307 F.2d 888.

On appeal from a summary judgment, the Court of Appeals should view the case from a standpoint most favorable to the appellant and accept his allegation of fact as true, and assume a state of facts most favorable to him. On appeal from a summary judgment, the only question is whether the allegations of the party against whom it was rendered was sufficient to raise a material or genuine issue of fact. Poller v. Columbia Broadcasting System, 368 U.S. 464; Tracer Lab., Inc. v. Industrial Nucleonics Corporation, 313 F.2d 97; Libby v. L. J. Corporation, 247 F.2d 78.

The determination of what constitutes a "genuine issue as to any material fact" is often difficult. It has been said that an issue is material if the facts alleged are such as to constitute a legal defense or are of such nature as to effect the result of the action, or if the resolution of the issue is so essential that the party against whom it is resolved may not prevail. Keehn v. Brady Transfer and Storage Company, 159 F.2d 383; Fishman v. Teeter, 133 F.2d 222.

While a motion for summary judgment may be used by the defendant to assert the defense of the statute of limitations, the motion should be denied where only by trial on the facts could it be determined when plaintiff knew or should have known that he might have an actionable injury or case of action. Tracer Lab, Inc. v. Industrial Nucleonics Corporation, 313 F.2d 97, R. J. Reynolds Tobacco Company v. Hudson, 314 F.2d 776; Sheets v.

Burman, 322 F.2d 277.

The second sentence of Respondent's Memorandum of Points and Authorities (Clk. Tr. p. 10, lines 9-15) recites as follows:

"In the event that summary judgment is denied the defendant, as there is a serious question of whether or not the plaintiff's complaint is barred by the two year statute of limitations in the Federal Tort Claims Act, it would seem that this might well be a case where, with the Court's approval, a separate trial on the issue of the statute of limitations should be held." (emphasis added.)

It would appear that the Respondent concedes in the Memorandum of Points and Authorities that there is a "genuine issue as to any material fact".

III

CONCLUSION

From each of the foregoing, it is respectfully submitted that the Affidavit of Appellant in Opposition to Respondent's Motion for Summary Judgment when considered with the pleadings on file, established that there was one or more issues of fact to be determined by the trier of fact, so that the Motion for Summary Judgment should have been denied.

If, in fact, the Appellant has made admissions in the letters that are attached as exhibits to Respondent's Motion for Summary Judgment are inconsistent with his statements in his Affidavit in Opposition to the Motion for Summary Judgment, this situation does no more than raise an issue of fact, which makes a trial necessary.

Respectfully submitted,

JAFFE, OSTERMAN & SOLL

By: F. FILMORE JAFFE

Attorneys for Appellant

CERTIFICATE

I certify in connection with the preparation of this brief that I have examined Rules 18 and 19 of the United States Court of Appeals for the Ninth Circuit and that, in my opinion, the foregoing brief is in full compliance with those rules.

/s/ F. Filmore Jaffe

F. FILMORE JAFFE

FEB 14 1967

NO. 20551

IN THE UNITED STATES COURT OF APPEALS
FOR THE NINTH CIRCUIT

ROBERT DULAINÉ,

Appellant,

vs.

UNITED STATES OF AMERICA,

Appellee.

APPELLEE'S BRIEF

APPEAL FROM
THE UNITED STATES DISTRICT COURT
FOR THE SOUTHERN DISTRICT OF CALIFORNIA
CENTRAL DIVISION

MANUEL L. REAL,
United States Attorney,
FREDERICK M. BROSIO, JR.,
Assistant U. S. Attorney,
Chief, Civil Division,
M. MORTON FREILICH,
Assistant U. S. Attorney,

600 U. S. Court House,
312 North Spring Street,
Los Angeles, California 90012,

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MAY 5 1966

WM. B. LUCK, CLERK

Attorneys for Appellee,
United States of America.

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M. MORTON FREILICH,
Assistant U. S. Attorney,

600 U. S. Court House,
312 North Spring Street,
Los Angeles, California 90012,

Attorneys for Appellee,
United States of America.

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IN THE UNITED STATES COURT OF APPEALS
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vs.

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APPELLEE'S BRIEF

JURISDICTIONAL STATEMENT

Appellant brought an action, for malpractice under the Federal Tort Claims Act, against the United States Government, in the United States District Court, Southern District of California [R. 2-6 incl. entitled "Complaint . . ."]. ^{1/} Appellant claimed that the District Court had jurisdiction under 28 U.S.C. §1346(b). It is the Government's position that, since there was a failure to comply with the Federal Tort Claims Act statute of limitations, which is a jurisdictional prerequisite, the District Court lacked jurisdiction to entertain the action. Hungerford v. United States, 307 F.2d 99

^{1/} References to the Transcript of Record will be indicated "R". References to the Supplemental Transcript of Record will be indicated "S.R.". References to Appellant's Brief will be indicated by "Br.".

(9th Cir. 1962). The District Court granted Appellee's, Motion for Summary Judgment [R. 40] on the ground that the Federal Tort Claims Act two-year statute of limitations had run. Since the District Court's decision was final, this Court has jurisdiction to review said decision under 28 U. S. C. §1291.

STATEMENT OF THE CASE

A. Introduction.

The action is one for medical malpractice. The gravamen of the Complaint is that an operation performed on the Appellant at a Veterans Administration Hospital in September, 1956, was negligently performed resulting in personal injury to the Appellant. The Complaint was not filed until November 13, 1964 [R. 2-6 incl.].

B. Chronology of Pleadings.

On November 13, 1964, Appellant, Robert Dulaine, filed a Complaint in the above-captioned matter against the United States of America, under the Federal Tort Claims Act, 28 U. S. C. §1346(b) for damages resulting from malpractice [R. 2-6 incl.].

On February 24, 1965, Appellant filed Plaintiff's Answers to Request for Admissions [S. R.].

On March 5, 1965, Appellee filed an Answer to the Complaint [S. R.].

On April 29, 1965, Appellant filed Answers to Interrogatories [S. R.].

On July 16, 1965, Appellee filed a Motion for Summary Judgment and Memorandum of Points and Authorities, and Affidavit [R. 7, et seq.].

On August 18, 1965, Appellant filed his Opposition to Motion for Summary Judgment with Affidavits [R. 25, et seq.].

On August 24, 1965, the Court filed Findings of Fact and Conclusions of Law on Appellee's Motion for Summary Judgment [R. 36, et seq.] and based upon such Findings of Fact and Conclusions of Law granted Appellee's Motion for Summary Judgment [R. 40]. The Order granting Defendant's Motion for Summary Judgment was entered on August 25, 1965 [R. 40]. This appeal is instituted to review said Order [Br. 2].

ISSUES PRESENTED

1. Do Appellant's assertions in his Affidavit in Opposition to Appellee's Motion for Summary Judgment create a genuine material fact issue which would, therefore, have to be disposed of at a trial?

2. Does the recital of facts contained in the medical records in Appellee's Affidavit in support of Appellee's Motion for Summary Judgment [R. 7, et seq.] violate the hearsay rule?

3. Did the District Court rely on said alleged hearsay in granting Appellee's Motion for Summary Judgment?

SUMMARY OF ARGUMENT

Since Appellant was aware of each of the alleged acts of malpractice by May 19, 1960, his Complaint, which was not filed until November 13, 1964, was barred by the Federal Tort Claims Act two-year statute of limitations (28 U.S.C. §2401(b)).

Appellant's assertions pertaining to his being unaware of the malpractice [Br. 5-9 incl.] are either immaterial or too incredible to be accepted by reasonable minds, in view of other evidence in the record. Such assertions, therefore, do not create a genuine material fact issue.

Appellee's recital of the facts contained in the medical records in Appellee's Affidavit in support of Appellee's Motion for Summary Judgment [R. 22, et seq.] does not violate the hearsay rule because medical records constitute an exception to the hearsay rule. Furthermore, the Court did not rely on said medical records in its Conclusions of Law and Findings of Fact. Furthermore, Appellant waived any hearsay objections that he might have had by failing to object in the Court below.

ARGUMENT

I

ALLEGED ACTS OF MALPRACTICE

The particular acts of malpractice upon which the Complaint is based are set forth in Plaintiff's Answer to Defendant's Interrogatory No. 2 [Plaintiff's Answer to Defendant's Interrogatory No. 2, S. R.].

Plaintiff's first allegation is that the negligence consisted of an improper technique in performing an aortogram (a pre-operative procedure) resulting in the failure to diagnose a second aneurysm or fistula, one having admittedly been diagnosed [Plaintiff's Answer to Defendant's Interrogatory No. 2, S. R. , and Plaintiff's March 26, 1957, letter, p. 3, Exhibit "A" to Request for Admission No. 1, S. R.]. Although Plaintiff in his Answer to said Interrogatory does not say that the reason why he is complaining of the defective aortogram is because of a failure to diagnose the second aneurysm or fistula, that would appear to be the reasonable inference [Plaintiff's March 26, 1957, letter, pp. 3 & 4, Exhibit "A" to Request for Admission No. 1, S. R.]. Said letter reveals that one fistula was discovered prior to the September, 1956, operation and that the second fistula was not discovered until said operation.

Appellant's second allegation of negligence involves the cutting of a rent in the common iliac vein and the ligation of the common iliac vein, the hypogastric vein, the external iliac vein,

and one of the large gluteal branches of the iliac vein [Plaintiff's Answer to Defendant's Interrogatory No. 2, S. R.].

Appellant's third allegation of negligence involves injury to the throat during surgery affecting his voice and speech [Plaintiff's Answer to Defendant's Interrogatory No. 2, S. R.].

All of the said alleged negligent acts occurred at or before the time the operation was performed in September of 1956 [Plaintiff's Answer to Defendant's Interrogatory No. 3, S. R. , and Plaintiff's Answer to Defendant's Interrogatory No. 2(g), S. R.].

II

APPELLANT WAS AWARE OF EACH NEGLIGENT ACT BY MAY 19, 1960.

Within a year after said operation of September, 1956, Appellant was aware of each act of alleged malpractice and of every adverse effect alleged to be a result thereof with the possible exception of the throat problem.

By March 26, 1957, Appellant was aware that there were two fistulas and that the aortogram had failed to disclose two fistulas [Appellant's letter of March 26, 1957, p. 3, Exhibit "A" to Request for Admission No. 1, S. R.].

By March 26, 1957, Appellant was aware that the main vein to the left leg had been cut and tied off [Appellant's March 26, 1957, letter, p. 4, Exhibit "A", cited supra, S. R. , and Appellant's June 6, 1957, letter, p. 3, Exhibit "C" to Request for Admission No.

3, S. R.]. A tying off of the main iliac vein necessarily involves a tying off of the other veins mentioned by Appellant as they are subsidiary to and lower than the main vein and dependent thereon [See Dorland's Illustrated Medical Dictionary, 23rd Edition, Plate XLIX].

By March 14, 1960, Appellant was aware of the alleged injuries to his throat [Appellant's March 14, 1960, letter, pp. 3 & 4, Exhibit "D" to Request for Admission No. 4, S. R.].

III

APPELLANT WAS AWARE OF ALL OF THE ADVERSE EFFECTS OF THE ALLEGED MAL- PRACTICE BY MAY 19, 1960.

By March 26, 1957, Appellant was aware of the adverse effects of the alleged acts of malpractice, and was, of course, aware of the underlying acts allegedly constituting malpractice. By March 26, 1957, Appellant was aware of the adverse effects involving the aforesaid main vein in the left leg, and was aware of the effects of the defective technique in performing the aortogram which resulted in the failure to diagnose the fistulas [Appellant's March 26, 1957, letter, pp. 3 & 4, Exhibit "A", cited supra, S. R., and Appellant's March 6, 1957, Application for Compensation, pp. 1 & 2, Exhibit "B" to Request for Admissions No. 2, S. R., and Appellant's June 6, 1957, letter, pp. 3 & 4, Exhibit "C" to Request for Admissions No. 3, S. R.].

At least by March 14, 1960, Appellant was aware of the alleged injuries to Appellant's throat [Appellant's March 14, 1960,

letter, pp. 3 & 4, Exhibit "D" to Request for Admissions No. 4, S. R.].

By May 19, 1960, Appellant had reached the firm conclusion that malpractice had taken place in connection with the said operation of September, 1956 [Appellant's May 19, 1960, letter, pp. 2 & 3, Exhibit "E" to Request for Admission No. 5, S. R.].

The Complaint herein was not filed until November 13, 1964 [R. 2].

IV

THE STATUTE OF LIMITATIONS COMMENCED TO RUN ON OR BEFORE MAY 19, 1960.

The two-year statute of limitations under the Federal Tort Claims Act (28 U. S. C. §2401(b)) began to run when the Appellant discovered, or, when in the exercise of reasonable diligence, Appellant should have discovered, the acts constituting the alleged malpractice.

Quinton v. United States, 304 F.2d 234

(5th Cir. 1962);

Hungerford v. United States, 307 F.2d 99

(9th Cir. 1962);

Brown v. United States, 353 F.2d 578

(9th Cir. 1965).

It is, therefore, apparent that the statute of limitations commenced to run by May 19, 1960, and that the filing of the

Complaint on November 13, 1964, was untimely.

V

REFUTATION OF APPELLANT'S CLAIMS OF
ERROR.

A. Appellant's Hearsay Objection.

Appellant complains that the Affidavit of Morton H. Boren in support of Appellee's Motion for Summary Judgment [R. 22, et seq.] reciting facts contained in Appellant's medical records, contained hearsay statements which should not have been considered in determining a Summary Judgment Motion [Br. 4].

The Findings of Fact [R. 36, et seq.] did not rely upon Boren's aforesaid Affidavit. The Findings of Fact were based entirely upon Appellant's pleadings and documents [R. 36, et seq.].

Furthermore, medical records come within an exception to the hearsay rule under the Business Records Rule, 28 U.S.C. §1732. See McCormick on Evidence, Section 290, pp. 609, et seq. Also see Rule 44, Federal Rules of Civil Procedure which establishes that an official record is an exception to the hearsay rule. The medical records in the instant case are Veterans Administration Records and are, therefore, official records.

Since the record fails to disclose a hearsay objection to the said Affidavit, such an objection has been waived and cannot be raised for the first time on an appeal. See McCormick on Evidence,

B. Appellant's Assertions Do Not Create
 Genuine Material Fact Issues.

Appellant argues [Br. 5-9 incl.] that there were sufficient facts stated in Appellant's Affidavit opposing Appellee's Motion for Summary Judgment to raise a genuine material issue of fact, and, therefore, the granting of Appellee's Motion for Summary Judgment, was erroneous. Appellant has placed in his brief those portions of Appellant's Affidavit in opposition to Appellee's Motion for Summary Judgment which Appellant argues raised genuine material fact issues [Br. 5-9 incl.].

An analysis in detail of Appellant's aforesaid assertions establishes that no genuine issue as to any material fact exists in the instant case. Appellant's aforesaid assertions pertaining to his being unaware of the malpractice are conclusionary or immaterial or incredible. Such assertions, therefore, do not raise an issue of credibility which should be heard at a trial. There is, therefore, in the instant case, no genuine issue of material fact.

To defeat a summary judgment movant, who has otherwise sustained his burden, a party opposing a motion must present facts proper in form, not conclusions. Dickheiser v. Pennsylvania R. R. (E.D. Pa. 1945), 9 F. R. Serv. 15a21, Case 1, 5 F. R. D. 5, aff'd. (3rd Cir. 1946), 155 F.2d 266, cert. denied (1947), 329 U. S. 808, 67 S.Ct. 620, 91 L.Ed. 689.

The opposing party's facts must be material. Nahtel Corp. v. West Virginia Pulp & Paper Co. (2nd Cir. 1944), 141 F.2d 1. The facts must be of a substantial nature, Bidler & Bookmyer v. Universal Ins. Co. (2nd Cir. 1943), 134 F.2d 828, 831; not fanciful, Dewey v. Clark (D.C. Cir. 1950), 180 F.2d 766, 772; nor frivolous, De Luca v. Atlantic Ref. Co. (2nd Cir. 1949), 176 F.2d 421, 423; nor gauzy, Sabin v. Home Owners Loan Corp. (10th Cir. 1945), 151 F.2d 541, 542, cert. denied (1946), 328 U.S. 840, 66 S.Ct. 1011, 90 L.Ed. 1615; nor merely casting suspicion, Banco de Espana v. Federal Reserve Bank (S.D. N.Y. 1939), 28 F.Supp. 958, 973, aff'd. (2nd Cir. 1940), 114 F.2d 438.

"To proceed to Summary Judgment, it is not sufficient that the Judge may not credit testimony pro-offered on a tendered issue. It must appear that there is no substantial evidence on it, that is, either that the tendered evidence is in its nature too incredible to be accepted by reasonable minds, or that conceding its truth, it is without legal probative force." Whitaker v. Coleman (5th Cir. 1940), 115 F.2d 305, 306.

"The above test has been applied and often quoted. Evidence, then, that is too incredible to be accepted by reasonable minds does not raise an issue of credibility. Conversely, if the evidence is such that the jury would not be at liberty to disbelieve it, no issue of credibility is present." Moore's Manual -- Federal Practice and Procedure, Moore and Vestal, 1962 1 Vol. Ed., p. 1295; Camerlin v. New York Cent. R. R. (1st Cir. 1952), 199 F.2d 698; Minor v. Washington Terminal Co. (D.C. Cir. 1950), 180 F.2d 10, 12; Surkin v. Charteris (5th Cir. 1952), 197 F.2d 77.

Appellant's first such assertion is that he was unaware of malpractice involving the rent in the main vein involving his left leg until late November, 1962 [Br. 5]. Such an assertion is incredible. By March 26, 1957, Appellant knew that the main vein, during the September 1956 operation had been "inadvertently cut . . . causing many complications" [March 26, 1957, letter, p. 4, Exhibit "A", cited supra]. By March 6, 1957, Appellant knew that the vein was ligated and that thrombophlebitis had set in [Appellant's March 6, 1957, Application for Compensation, p. 1, Exhibit "B", cited supra, S. R.]. By June 6, 1957, Appellant realized that the rent and ligation resulted in his having a bad left leg, and that the

Veterans Administration owed him a settlement for the rent and the ligation [Appellant's June 6, 1957, letter, pp. 1, 3 & 4 Exhibit "C", cited supra, S. R.]. By May 19, 1960, Appellant reached the firm conclusion that malpractice was perpetrated in connection with the rent and ligation of the main vein affecting his left leg [Appellant's May 19, 1960, letter, p. 3, Exhibit "E", cited supra, S. R., and Appellant's November 13, 1960, letter, pp. 1 & 2, Exhibit "G" to Request for Admission No. 7, S. R.].

Appellant's next assertion is that he didn't know that facts were omitted in his medical records until 1964 [Br. 5 & 6, beginning with last paragraph on p. 5]. Such an assertion is immaterial. The dispositive issue is Appellant's awareness of malpractice. If Appellant were aware of the acts of malpractice, he was aware of the acts of malpractice. The mere fact of omissions in medical records does not refute the fact that Appellant was aware.

Appellant's next assertion deals with omissions in a document pertaining to foreign bodies [Br. 6]. Such an assertion is immaterial for the reasons stated above. An omission in a document does not prove Appellant's lack of awareness of malpractice. Appellant's assertions regarding omissions do not refute other evidence establishing Appellant's awareness of malpractice.

Appellant's next assertion again deals with an omission to list facts concerning the rent in his left leg [Br. 6]. Appellant also complains that the Government concealed certain facts pertaining to said left leg [Br. 6]. Again such assertions are immaterial as they do not refute evidence establishing that Appellant was aware

of malpractice by 1960. As set forth above, Appellant reached the firm conclusion that malpractice had been perpetrated in connection with his left leg by May 19, 1960. [Appellant's May 19, 1960, letter, pp. 2 & 3, Exhibit "E", cited supra]. Since Appellee has established that Appellant was aware of malpractice perpetrated in connection with his left leg, the Government's alleged concealment of facts and omissions to list do not show Appellant's lack of awareness, and Appellant's assertions are therefore immaterial. If Appellant were aware of malpractice, then he was aware, regardless of the Government's alleged concealments and omissions to list.

Appellant's next assertion again deals with omissions in documents and the concealment of a malpractice form [Br. 7]. Such assertions are again immaterial because they do not refute the fact that Appellant possessed knowledge of alleged malpractice by 1960.

Appellant's next assertion is that he did not discover the improper technique in performing an aortogram until 1962 [Br. 8]. The reasonable implication appears to be that the improper aortogram resulted in a failure to diagnose aneurysms or fistulas and that that is why Appellant is complaining of the improper aortogram [Appellant's March 26, 1957, letter, pp. 3 & 4, Exhibit "A", cited supra, and Plaintiff's Answer to Defendant's Interrogatory No. 2, S. R.]. Such an assertion is incredible in view of other evidence establishing that Appellant was aware of said improper technique and its consequences by March 26, 1957 [Appellant's March 26, 1957, letter, p. 3, Exhibit "A", cited supra, and Appellant's

June 6, 1957, letter, pp. 2 & 3, Exhibit "C", cited supra, S. R.].

Appellant's next assertion deals with the Government's alleged failure to diagnose aneurysms or fistulas. Appellant was aware of the existence of the aneurysms or fistulas and of the fact that they should have been diagnosed and repaired by March 26, 1957 [Appellant's March 26, 1957, letter, p. 4, Exhibit "A", cited supra, S. R.]. Appellant states in said March 26, 1957, letter that the fistulas should have been repaired and, inferentially, diagnosed in 1945 when he was first wounded. [Appellant's March 26, 1957, letter, p. 4, Exhibit "A", cited supra, S. R.]. Appellant states that the fistulas were instead not repaired until October, 1956 [Appellant's March 6, 1957, Application for Compensation, p. 2, Exhibit "B", cited supra, S. R.]. Appellant was, therefore, aware of the alleged malpractice pertaining to the fistulas by March 26, 1957.

Appellant's next assertion deals with his left leg and the failure of the Veterans Administration to admit that ligations were made, until 1963 [Br. 8]. Such an assertion is immaterial. The Government's failure to make an admission does not refute Appellant's awareness of malpractice by 1960. It has already been established that Appellant was aware of the alleged malpractice concerning his left leg by May 19, 1960 [Appellant's May 19, 1960, letter, pp. 2 & 3, Exhibit "E", cited supra, S. R.].

Appellant's last assertion is the conclusionary statement that he was unaware of malpractice until the latter part of November, 1962 [Br. 9]. Such an assertion is incredible in view of other

evidence. To again refer to such evidence would be unnecessary and repetitious.

Justice Cardoza's statement bears repetition:

"The very object of a Motion for Summary Judgment is to separate what is formal or pretended . . . from what is genuine and substantial, so that only the latter may subject a suitor to the burden of a trial." Richard v. Credit Susse (1926), 242 N. Y. 346, 152 N. E. 110.

CONCLUSION

For the reasons set forth above, it is respectfully submitted that the Order of the District Court granting Appellee's Motion for Summary Judgment and denying the relief prayed for in Appellant's Complaint, should be affirmed.

Respectfully submitted,

MANUEL L. REAL,
United States Attorney,

FREDERICK M. BROSIO, JR.,
Assistant U. S. Attorney,
Chief, Civil Division,

M. MORTON FREILICH,
Assistant U. S. Attorney,

Attorneys for Appellee,
United States of America.

CERTIFICATE

I certify that in connection with the preparation of this brief, I have examined Rules 18 and 19 of the United States Court of Appeals for the Ninth Circuit, and that, in my opinion, the foregoing brief is in full compliance with those rules.

/s/ M. Morton Freilich

M. MORTON FREILICH

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FOR THE NINTH CIRCUIT

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Defendant and Respondent.

APPELLANT'S CLOSING BRIEF

APPEAL FROM
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FOR THE SOUTHERN DISTRICT OF CALIFORNIA
CENTRAL DIVISION

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JUL 11 1966
WM. B. LUCK, CLERK

JAFFE, OSTERMAN & SOLL

By: F. FILMORE JAFFE

6380 Wilshire Boulevard

Suite 900

Los Angeles, California 90048

Attorneys for Appellant

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JAFFE, OSTERMAN & SOLL

By: F. FILMORE JAFFE

6380 Wilshire Boulevard

Suite 900

Los Angeles, California 90048

Attorneys for Appellant

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IN THE UNITED STATES COURT OF APPEALS
FOR THE NINTH CIRCUIT

ROBERT DULAINÉ,

Plaintiff and Appellant,

vs.

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Defendant and Respondent.

APPELLANT'S CLOSING BRIEF

PRELIMINARY STATEMENT

The Appellee, in its brief, sets forth three issues which this Court is called upon to determine. Appellant's brief will treat with his position on those issues presented by the Appellee.

I

DO APPELLANT'S ASSERTIONS IN HIS AFFIDAVIT IN OPPOSITION TO APPELLEE'S MOTION FOR SUMMARY JUDGMENT CREATE A GENUINE, MATERIAL FACT WHICH WOULD, THEREFORE, HAVE TO BE DISPOSED OF AT A TRIAL?

The foregoing query must be answered in the affirmative.

The two-year Statute of Limitations under the Federal Tort

Claims Act (28 U. S. C. §2401(b)) began to run when the Appellant discovered, or, when in the exercise of reasonable diligence, Appellant should have discovered, the acts constituting the alleged malpractice. Brown v. United States, 353 F.2d 578.

The question now presented is when did the Appellant discover, or, in the exercise of reasonable diligence, should he have discovered, the acts constituting the alleged malpractice? The Appellant states under oath in his Affidavit in Opposition to Motion for Summary Judgment (Clk. Tr. pp. 25-34), and as is set out in his Opening Brief, pages 5 to 9, that he was not aware of the malpractice until he learned the true facts late in November 1962, when his medical record of the Veterans Administration Hospital was released to him and he was able to examine the medical records. It is academic that facts asserted by the party opposing the Motion for Summary Judgment supported by affidavits or other evidentiary material, must be taken as true. Janek v. Celebrezze, 336 F.2d 828; Kilfoyle v. Wright, 300 F.2d 626.

In support of Appellee's Motion for Summary Judgment, Appellee alludes to a letter dated March 26, 1957, attached as Exhibit "A" to Request for Admissions #1. If, in fact, the Appellant made admissions in said letter which are inconsistent with the statements in his affidavit, concerning the time Appellant discovered the acts constituting the alleged malpractice, this situation, the Courts say, do no more than raise an issue of fact, which makes a trial necessary. Eagle Oil & Refining Co. v. Prentice, 19 Cal.2d 553.

The contraverted allegations as to when Appellant discovered, or, in the exercise of reasonable diligence, should have discovered the acts constituting the alleged malpractice, can only be resolved by a trial on the merits, and not by summary judgment. Free v. Bland, 369 U.S. 663; Sheets v. Burman, 322 F.2d 277; R. J. Reynolds Tobacco Company v. Hudson, 314 F.2d 776.

II

DOES THE RECITAL OF FACTS CONTAINED IN THE MEDICAL RECORDS IN APPELLEE'S AFFIDAVIT IN SUPPORT OF APPELLEE'S MOTION FOR SUMMARY JUDGMENT VIOLATE THE HEARSAY RULE?

The foregoing must be answered in the affirmative.

Rule 56(e) provides that supporting and opposing affidavits shall be made on personal knowledge, shall set forth such facts as would be admissible in evidence, and shall show affirmatively that the affiant is competent to testify as to the matters stated therein. Jameson v. Jameson, 176 F.2d 58.

In support of Appellee's Motion for Summary Judgment, Morton H. Boren, an Assistant United States Attorney, filed his affidavit (Clk. Tr. p. 22), wherein he states,

- "2. That he has reviewed the medical records of the Veterans Administration relating to the medical treatment rendered to plaintiff.
- "3. That the plaintiff's medical records contain the following facts:

"(a) That on February 2nd, 1959, the plaintiff was discharged as a patient from the Veterans Administration Hospital, West Los Angeles, California,

"(b)

"(c)"

It is obvious that the Assistant United States Attorney cannot competently testify as to what the Appellant's medical record discloses. It is also obvious that a recitation in the affidavit of Morton H. Boren as to what Appellant's medical records contain, are merely hearsay statements which will not be considered in determining the Motion for Summary Judgment. Dyer v. MacDougal, 201 F.2d 265; Jameson v. Jameson, 176 F.2d 58.

The medical records of the Appellant are the best evidence of what the records contain, and should have been submitted with the affidavit of the Custodian of Records of the Veterans Administration Hospital, indicating that the records submitted are the records of the Veterans Administration Hospital, and are the medical records of the Appellant.

III

DID THE DISTRICT COURT RELY ON THE
ALLEGED HEARSAY IN GRANTING APPEL-
LEE'S MOTION FOR SUMMARY JUDGMENT?

The foregoing question must be answered in the affirmative.

As above set forth, the affidavit of Morton H. Boren contains the fact taken from the Appellant's medical records, that "on February 2nd, 1959, Appellant was discharged as a patient from the Veterans Administration Hospital, West Los Angeles, California". The District Court, in granting the Motion for Summary Judgment and in making its Findings of Fact and Conclusions of Law, stated in Finding No. V, that "on February 2nd, 1959, plaintiff was discharged as a patient from the Veterans Administration Hospital at Sawtelle, California". This fact was not disclosed in any affidavit other than the affidavit of Morton H. Boren, alluded to above. It is further evident that the District Court did rely on said alleged hearsay in granting Appellee's Motion for Summary Judgment.

IV

CONCLUSION

On appeal from a Summary Judgment, the Court of Appeals should view the case from a standpoint most favorable to the Appellant, and accept his allegations of fact as true, and assume a state of facts most favorable to him. Carr v. City of Anchorage, 243 F.2d 482; Weisser v. Mersam Shoe Corp., 127 F.2d 344; Billeaudeau v. Temple Associates, 213 F.2d 707.

On appeal from a summary judgment, the only question is whether the allegations of the party against whom it was rendered, were sufficient to raise a material or genuine issue of fact.

The Court must accept as true the statement contained in Appellant's affidavit in opposition to the Motion for Summary Judgment, that he did not discover the alleged malpractice until the latter part of November 1962. That contraverted fact raises an issue of fact which can only be resolved by the trial on the merits and not by summary judgment.

Judgment should be reversed so that the Appellant may have his day in Court.

Respectfully submitted,

JAFFE, OSTERMAN & SOLL

By: F. FILMORE JAFFE

Attorneys for Appellant.

CERTIFICATE

I certify in connection with the preparation of this brief that I have examined Rules 18 and 19 of the United States Court of Appeals for the Ninth Circuit and that, in my opinion, the foregoing brief is in full compliance with those rules.

/s/ F. Filmore Jaffe

F. FILMORE JAFFE

FEB 14 1967

No. 20552 /

United States Court of Appeals

FOR THE NINTH CIRCUIT

ISLAND AIRLINES, INCORPORATED, *Petitioner,*

v.

CIVIL AERONAUTICS BOARD, *Respondent.*

BRIEF FOR THE PETITIONER

GEORGE F. GALLAND
G. NATHAN CALKINS
AMY SCUPI

GALLAND, KHARASCH, CALKINS
& LIPPMAN
1824 R Street, N.W.
Washington, D. C. 20009
Attorneys for Petitioner

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WM. B. LUCK, CLERK

February 23, 1966



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United States Court of Appeals

FOR THE NINTH CIRCUIT

No. 20552

ISLAND AIRLINES, INCORPORATED, *Petitioner*,

v.

CIVIL AERONAUTICS BOARD, *Respondent*.

BRIEF FOR THE PETITIONER

I. JURISDICTION

Jurisdiction of this proceeding to review an order of the Civil Aeronautics Board (CAB) rests in this Court under § 1006 of the Federal Aviation Act of 1958 (the Act), 49 U.S.C. 1486—petitioner (Island Airlines) being a Hawaii corporation with its principal place of business in Honolulu.

II. STATEMENT OF THE CASE

The petition requests this Court to review and nullify a CAB order (R. 167-70) denying Island Airlines exemption from economic regulation by the Federal Government under Title IV of the Act, 49 U.S.C. 1371 ff. Island sought the exemption by a petition (R. 1-35) addressed to the CAB under § 416(b) of the Act, 49 U.S.C. 1386(b).¹ The CAB order of denial (R. 167-70) was served October 12, 1965.

Island has been authorized by the State of Hawaii to carry passengers by air solely from points in Hawaii to other points in Hawaii—i.e., to carry intrastate passengers

¹ The cited sections and others deemed pertinent are printed in the appendix.

exclusively. Its current authority is an order of the Hawaii Public Utilities Commission issued February 1, 1965 (R. 9-10). Under a previous order of the same Commission, Island operated during 1963 in Hawaiian *interisland* but *intrastate* commerce. It has not, however, operated since 1963 because its operation has been enjoined by the United States District Court for Hawaii. The injunction issued at the suit of the CAB and was affirmed by this Court on October 29, 1965 in *Island Airlines, Inc. v. C.A.B.*, 352 F.2d 735.

This decision establishes that (a) the ocean channels between the islands comprising the State of Hawaii are international waters; (b) the United States can assume jurisdiction of flights which traverse such channels enroute solely between places in Hawaii; and (c) the United States *has* assumed such jurisdiction in the Federal Aviation Act.

The exemption petition to the CAB was framed in recognition of these basic principles. The petition asserted, however, a distinction between the *constitutional power* of the Federal Government to regulate intrastate commerce over the high seas, and the *administrative propriety* of such regulation by the CAB under the standards which the Act establishes—including standards for exemption. That distinction was not involved in the previous *Island* case.²

² The decision said (352 F. 2d at 742):

“Appellant urges that the federal agencies and the courts should refrain from exercising jurisdiction, in view of the Hawaiian Supreme Court’s decision, upholding the Hawaiian Public Utilities Commission’s jurisdiction. (Application of Island Airlines, Inc., 47 Haw. 1, 384 P. 2d 536 (1963).) Such position, in our view, begs the fundamental question. If the flights are intrastate, then of course, the federal courts should not permit the C.A.B. to require a certificate, but conversely, if the ‘channels’ are high seas, then flight over them should and must be subject to the C.A.B.’s authority. This general principle of the supremacy of federal control over interstate and high seas flights must prevail, if the facts support it, over the paramount importance to the Hawaiian economy of inter-island air transportation.”

The Court was here treating the CAB as the instrument of federal supremacy. The quoted language had no bearing on the problem of administration forbearance, since the discretion of the CAB to issue exemptions in proper cases had not been invoked.

The previous case was litigated and decided as if the CAB were *required* to act whenever federal power could be sustained. This, however, is not what the Act provides. It looks not in one direction but in two: towards regulation in many instances; towards exemption in some. Thus, while § 401, 49 U.S.C. 1371, provides that no air carrier “shall engage in any air transportation” (as defined) without a CAB certificate, § 416(b) empowers the agency to “exempt from the requirements of this title or any provision thereof . . . any air carrier or class of air carriers” if it finds that enforcement would be an “undue burden . . . by reason of the limited extent of, or unusual circumstances affecting, the operations of such air carrier or class of air carriers and is not in the public interest.”

The question whether Island or other carriers of its class should be exempted from regulation has not heretofore come before this Court—nor could it have without prior submission to the CAB. Accordingly, Island filed its CAB exemption petition upon securing rate and operating authority under the State P.U.C. order of February 25, 1965. Island sought exemption not for itself alone but also for “others similarly situated” (R. 2). Its petition was supported by a resolution of the Hawaii Senate (R. 30-32); by a concurrent resolution of both houses of the State’s legislature (R. 33-35); and by the Boards of Supervisors of Maui and Kauai counties.³ The legislative resolutions were attached to and filed with and as a part of Island’s petition. The resolutions requested the CAB to establish a special class of “Hawaiian Intrastate Carriers” (comprising those carriers in Hawaii who were federally regulated solely because their flight paths cross channels of the high seas in interisland flights) and to exempt them from Title IV regulation.

³ The Maui petition is in the record (pp. 158-59). The Kauai petition is not, but the CAB transmitted a copy to the Court by letter of January 20, 1965, which authorized the Court to refer to it.

The CAB received answers to the Island petition from Hawaiian (R. 38-142) and Aloha (R. 143-157) Airlines. Those answers tendered issues of fact which Island had no opportunity to contest. On October 11, 1965, the CAB, without a hearing and without announcing its procedure, denied the Island petition by the order here under review, which rested in large part on facts asserted by Aloha and Hawaiian airlines in unverified pleadings, but never proved. By identical letters of October 12, 1965,⁴ the CAB denied the petitions of the Hawaii legislature solely on the basis of the order which had denied Island's petition.

III. SPECIFICATION OF ERRORS

A. Denial of exemption was arbitrary and capricious, and constituted an abuse of discretion and legal error in view of the purposes and policies of the Federal Aviation Act and the undisputed facts of record.

B. Denial of exemption was unlawful because it extinguished Hawaii's power over its intrastate commerce in derogation of Hawaii's "equal footing" with other states under the U.S. Constitution and the Hawaii Statehood Act.

C. The order under review is (1) unsupported by substantial evidence, and (2) based on evidence received without a hearing or other lawful fact-finding procedure in violation of sections 4 and 5 of the Administrative Procedure Act (5 U.S.C. 1003, 1004) and the due process requirement of Amendment 5 to the U.S. Constitution.

⁴ Available to the Court by virtue of the CAB letter of January 20, 1966, and annexed as Exhibit A to Island's Petition to this Court.

IV. ARGUMENT

A. DENIAL OF ISLAND'S EXEMPTION PETITION WAS ARBITRARY, CAPRICIOUS, AN ABUSE OF DISCRETION, AND LEGALLY WRONG UNDER THE FEDERAL AVIATION ACT.

Agency action which is "arbitrary, capricious, an abuse of discretion, or otherwise not in accordance with law" is subject to judicial correction under § 10(e) of the Administrative Procedure Act, 5 U.S.C. 1009(e).

The standards for testing abuse of discretion fall short of exactness but in general demand that agency action, to survive review, fall within the bounds of good sense and sound reason. *National Labor Relations Board v. Guernsey-Muskingum Electric Co-op, Inc.*, 285 F.2d 8, 11 (6th Cir., 1960) states:

"There is no exact measure of what constitutes abuse of discretion. It is more than the substitution of the judgment of one tribunal for that of another. Judicial discretion is governed by the situation and circumstances affecting each individual case. 'Even where an appellate court has power to review the exercise of such discretion, the inquiry is confined to whether such situation and circumstances clearly show an abuse of discretion, that is, arbitrary action not justifiable in view of such situation and circumstances.' *Hartford-Empire Co. v. Obear-Nester Glass Co.*, 8 Cir., 95 F.2d 414, 417."

Except where agency action is held totally non-reviewable because *conclusively* committed to agency discretion⁵ the agency is held to "a sound discretion exercised in a

⁵ See *Ferry v. Udall*, 336 F. 2d 706, 711 (9th Cir., 1964), cert. denied 381 U.S. 904, where this court held that the refusal of the Secretary of the Interior (for any reason or none) to sell public lands, was non-reviewable, as a matter of substantive law. Action of the type in question, denying a governmental benefit, is commonly held to be further beyond the reach of a reviewing court than action which "denies a vested property right or which imposes a substantial obligation or burden." *Hamel v. Nelson*, 226 F. Supp. 96, 99 (N.D. Calif., 1963), citing *Davis*, *Administrative Law* (1958 ed.), § 28.19.

manner that is not violative of due process.” *First Nat. Bank of Smithfield v. First Nat. Bank of E.N.C.*, 232 F. Supp. 725, 730 (E.D. N.C., 1964). A grant of discretion does not mean “unfettered discretion.” *Freeman v. Brown*, 342 F. 2d 205, 212-13 (5th Cir., 1965); *Vucinic v. U. S. Immigration & Naturalization Service*, 243 F. Supp. 113, 116 (D.C. Ore., 1965). For the CAB in passing on exemption applications, the question has been answered by *American Airlines v. Civil Aeronautics Board*, 235 F.2d 845, 853 (D.C. Cir., 1956) holding that the statute “requires [the Board] to find, not in conclusory fashion in the statutory language but in such fashion that a reviewing court can test the validity of the finding.” We contend that the CAB has thwarted the reviewing function as to findings which it should have made but failed to make, and invited reversal of those it did make because they were clearly wrong.

1. The Petition to the CAB

Island’s petition to the Board for exemption rested on these major propositions:

- a. Hawaii is now a state.
- b. Island has been authorized, under a rate order of the Hawaii Public Utilities Commission, to engage in the transportation of passengers solely between places in Hawaii—i.e., in commerce which is in fact and in substance intrastate (R. 1).
- c. Island proposes to operate only as so authorized (R. 4, 9-10, 13).
- d. The type of operation authorized for and proposed by Island would be subject to state regulation exclusively in every state of the Union other than Hawaii (R. 1-2).
- e. Federal jurisdiction of Hawaii’s intrastate commerce rests entirely on the geographic happenstance that Hawaii is an island archipelago so that planes in flight from island to island must transit ocean channels

more than six miles wide (R. 1-2). Island, however, will carry no passengers in commerce "with foreign Nations" or "among the several states" or "with the Indian Tribes" (Constitution, Art. 1, § 8).

f. Despite the technically international status of interisland channels, the United States, through the Federal Aviation Administrator, has treated the Hawaiian archipelago for practical purposes as continuous United States territory by designating federal airways between all of the Hawaiian islands. Such designation is permissible only in "air space of the United States" (R. 10-12).

g. Hawaii stands in peculiar need of power to regulate and promote its local air commerce because air travel is the only available means of inter-island passenger travel (R. 25). Its total dependence on air transportation has been recognized by the Supreme Court of Hawaii (R. 8), the CAB (R. 14-16), and the Hawaii legislature (R. 24, 30-35).

h. The CAB has in the past exercised its exemption power in conformity with the principles advocated by Island (R. 23-24).

i. The law encourages deference towards state sovereignty where federal jurisdiction rests on a purely technical basis (R. 20-24).

j. The only possible ground of federal interest in intra-Hawaii air service is the protection of two existing air carriers from competition. Neither of such carriers, however, has ever met the test of public convenience and necessity which the CAB demands that Island pass before engaging in Hawaii's local commerce (R. 13).⁶

⁶ Hawaiian Airlines was certified as a grandfather carrier. Aloha Airlines was certified to provide competition with Hawaiian. Both events occurred when Hawaii was a territory and the federal government was the local governing authority, as is the state government today (R. 13-17).

2. The CAB Order of Denial

The CAB order denying exemption (R. 167-70) summarizes various contentions advanced by Island but neither analyzes nor refutes any of them. While *stating* that "Island has not made a sufficient showing . . ." (R. 168(a)),⁷ the CAB *decides* adversely to Island on the exclusive basis of two "facts" alleged in the answers of the presently-certified airlines but never made the subject of a hearing or any substitute procedure in which the facts (or their significance) could be tested.⁸ The first of such facts is that the federal government has spent over \$6,000,000 of subsidy on the interveners since 1949. The second is that the interveners would lose nearly \$5,000,000 in annual revenues to the proposed Island operation.⁹ "Under these circumstances," says the order, "it would not be in the public interest to grant exemption authority permitting a carrier or carriers to operate in direct competition with Aloha and Hawaiian." (R. 168(a)).

The order next rejects Island's contention that federal jurisdiction rested on a "technical" foundation (R. 168(b)). Rejection was based solely on a statement in the report of the Senate Insular Affairs Committee on the Hawaiian Statehood Act (R. 53) that the Federal Aviation Act "and other applicable Federal legislation" should continue to apply between places in Hawaii. We discuss these matters in inverse order.

⁷ Two pages are numbered 168. We designate them as 168(a) and 168(b).

⁸ The failure of the CAB to afford opportunity for Island to contest or refute the interveners' allegations is the subject of a separate assignment of error. See pages 34-38, below.

⁹ The CAB presumably knows and can notice officially the amount of subsidy paid; the precise sum (as distinguished from its legal effect) seems of minor importance, and we do not contest it. The findings on diversion, however, are strongly contested. They rest on nothing but estimates (in a lawyer's unverified pleading) and can in no sense be taken as evidence. *Minnesota Rate Cases* (*Simpson v. Shepard*), 230 U.S. 352 (1913). The estimates would have been attacked and rebutted had opportunity been afforded, and the rebuttal evidence would have included current CAB material in direct conflict with its conclusions here.

3. Senate Report on the Statehood Act

The relevant document is Senate Report 80, 86th Congress, 1st Session. The passage cited by the CAB is quoted in part in Hawaiian's answer (R. 53), to the effect above noted. The quoted passage was followed in the report by an approving reference (unmentioned by Hawaiian) to Interior Department memoranda set out in Appendix F to the report. The report invites two comments. First, a committee statement that a particular law and all "applicable" laws should continue to apply in accordance with their terms adds nothing to the general body of legal wisdom. Obviously an Act applies to whatever it applies to, but the germane point in relation to the Federal Aviation Act is that it embodies not only a program of regulation but also a program of exemption. The CAB is bound to administer both as sound policy may dictate.¹⁰ "If possible, all sections of the Act must be reconciled so as to produce a symmetrical whole." *Federal Power Commission v. Panhandle Eastern Pipeline Co.*, 337 U.S. 498, 514 (1949); *Richards v. United States*, 369 U.S. 1, 11 (1962).

Administrative bodies may not pick and choose their favorite statutory provisions or even their favorite statutes, but must heed the entire body of laws and policies which affect their functions. As stated in *Southern Steamship Co. v. N.L.R.B.*, 316 U.S. 31, 47 (1942):

"It is sufficient for this case to observe that the Board has not been commissioned to effectuate the policies of the Labor Relations Act so single-mindedly that it may wholly ignore other and equally important Congressional objectives. Frequently the entire scope of Congressional purpose calls for careful accommodation of one statutory scheme to another, and it is not too much to demand of an administrative body that it undertake

¹⁰ The CAB was recently reminded that even a presidential preference for a particular result could not control the performance of the Board's statutory duties. *Western Airlines, Inc. v. CAB*, 351 F. 2d 778, 782 (D.C. Cir., 1965)

this accommodation without excessive emphasis upon its immediate task.”

The CAB reasonably may be asked, under this doctrine, to accord a measure of recognition to the basic constitutional distribution of functions between the states and the nation by noting that states have presumptive power over intrastate commerce and that the commerce here involved is intrastate in every substantial sense. In any event, if agencies may be asked to sensitize themselves to the overtones of laws they do not administer, they are the more clearly required to apply as entireties the laws they do administer. No Congressional committee can extinguish that duty.

Our second observation on the Committee report is that even if the Committee could have foreclosed the issue of exemption, it made no such attempt. Any inference that the Committee was anti-exemption as regards intra-Hawaiian air commerce is dispelled by the memoranda which it cited approvingly in Appendix F to its report.¹¹ Those memoranda indicate: (i) that intrastate *maritime* commerce is of no federal concern;¹² (ii) that Hawaiian interisland transportation generally is local in the sense which admits of state regulation under *Wilmington Transportation Co. v. California R.R. Comm.*, 236 U.S. 151 (1915) (discussed in Island's petition, R. 19) if discrimination is avoided and Congress has not acted inconsistently;¹³ (iii) that Hawaii could tax the total gross receipts from interisland transportation even though it traversed the high seas;¹⁴ and (iv) Hawaii could tax sales of goods in interisland commerce even though they were to move across international waters in the course of delivery.¹⁵ All of

¹¹ U.S. Cong. & Admin. News, 86th Cong., 1st Sess., pp. 1408-11.

¹² *Id.*, p. 1408.

¹³ *Id.*, p. 1409.

¹⁴ *Id.*, p. 1410.

¹⁵ *Id.*, p. 1411.

these activities would, of course, be strictly forbidden if interisland transportation constituted interstate (or foreign) commerce in any substantive sense. *Covington & C. Bridge Co. v. Kentucky*, 154 U.S. 204 (1894); *Wabash, St. L. & P. Ry. Co. v. Illinois*, 118 U.S. 557 (1886); *Crandall v. Nevada*, 73 U.S. 35 (1868). Having thus established the slightness of the federal interest in interisland commerce, the Committee report cannot fairly be read in denigration of the Board's exemptive power.

4. Irrelevance of Subsidies and Losses

While the CAB's reliance on subsidy is great, explanation of its relevance is missing. The order said, relative to subsidy (and operating losses) only this (R. 168(a)):

"In addition, the Federal Government has a substantial interest in the problems of interisland air transportation, which could¹⁶ be adversely affected by the exemption requested. Since 1949 it has paid \$6,377,000 in subsidy to the two interisland carriers. Aloha estimates that Island's proposed service would divert \$1,000,000 annual revenue from Aloha, and Hawaiian estimates that the two subsidized carriers would lose an additional \$4,856,000 annually as a result of Island's service. These diversion estimates are based on Island's service alone, while the application presents the possibility of an even greater number of additional carriers in the market. Under these circumstances, it would not be in the public interest to grant exemption authority permitting a carrier or carriers to operate in direct competition with Aloha and Hawaiian."

The order contains no explanation as to how the public interest—present or future—is affected by a federal expenditure of \$6,377,000 over a past period of seventeen years. What the order implies is that since subsidy has been paid for many years, the public interest requires its continuance in perpetuity by excluding competitors who

¹⁶ "Could" rather than "would". The Board's propensity for fearing the worst is an inadequate substitute for findings of fact.

would serve the intra-Hawaiian trade unsubsidized. The CAB seems to be announcing that it can buy federal jurisdiction with a monetary grant and that jurisdiction so bought must roll eternally onward through its own momentum. Implicit in this position is the assumption that the public interest in maintaining federal jurisdiction is proportionate to the size of prior expenditures. From this follows the conclusion that big subsidies already paid call for big subsidies hereafter to be paid. A more inventively warped concept of the public interest would be hard to contrive.

The above-quoted excerpt switches in midpassage from past subsidies paid by the government to future losses predicted by the carrier beneficiaries. The relevance of these prophecies¹⁷ is obscure. If a relationship exists between future losses and future subsidies, it is undisclosed. If the CAB is suggesting that it has a commitment to match bigger losses with bigger subsidies regardless of circumstance, we again suggest that its concept of the public interest demands correction.

5. The Concept of Public Interest

(a) The Present Monopoly

The CAB order states three times, with prodigal monotony, that the exemption sought would not be in the public interest—without once confiding its official view of that exalted concept. We find a hint on the face of the order as to what the public interest *excludes*, viz.: competition with carriers which have received large subsidies for long periods, and competition with carriers who tout their corporate anemia by boasting of their chronic losses (R. 61). Some clues to the Board's affirmative philosophy may be sought with reward in the interveners' pleadings since the Board's order constitutes a summary adoption of

¹⁷ We continue to emphasize that they are only prophecies, and to contend that the Board could not lawfully accept them without supporting proof.

their contentions. A position deserving of bonus points for originality is Hawaiian's lament (R. 61) that Hawaiian and Aloha have experienced slow growth "due to the unique situation of having no surface traffic from which to divert passengers." With the euphemism sifted out, this means that Hawaiian and Aloha are stymied by the completeness of their monopoly and must therefore be saved from competitors on the ground that having no new worlds to conquer, they have none to share. The CAB agrees—and explains its agreement in terms of the public interest. Thus, in the Board's concept, the public interest means the preservation of monopoly.

Further, it means the preservation of monopoly for carriers whose own operations have never in any substantial sense met the current tests of the Act as to public convenience and necessity. Born in the days of federal overlordship of Hawaii as a territory, both carriers were held to be required in the interest of the island archipelago's *domestic* commerce—an interest which the Board lost with the passage of the statehood act. The jurisdiction which remains to it—either true interstate commerce or commerce of the fictitious variety which the Board would apply to bar petitioner—has never been applied to Hawaiian or Aloha. Hawaiian received a grandfather certificate in 1939 (R. 14). Aloha was later certified (1948) without subsidy solely because Hawaiian was a monopolist whose island public needed the benefits of competition (R. 14-15). Aloha was then subsidized (1951) to keep it alive as a competitor (R. 15-16)—all in the local interest of Hawaii as a territory. In 1955 the CAB imposed a service cut-back to conserve subsidy funds (R. 17-18)—whereupon the subsidy initially granted to promote service became the cause of its contraction and—in the present case—the excuse for depriving Hawaii of Island's economy service which the state wants and needs and which its government demands the right to sponsor.

We submit that the Board's approach is fatally defective when it overrides Hawaii's officially-expressed need for Island's service, in order to make competition-proof two carriers who have never passed the public convenience test in the past and are not asked to pass it here. In the CAB view, Hawaiian and Aloha have only to prove that, like Mt. Everest, they are there; and proving this, they render themselves—unlike Mt. Everest—impregnable. We should suppose that if monopoly is to be automatically equated with the public interest, proof should be demanded that, at the least, the monopoly involved was a good monopoly. Such proof is lacking here.

(b) The Effect of Statehood

When Hawaiian and Aloha were certified and subsidized, Hawaii was a territory and the United States stood in the relationship of *parens patriae*: the federal government was the local government of Hawaii. The CAB certification and subsidy proceedings relative to Hawaiian and Aloha were conducted and decided in terms of Hawaii's local needs as appraised by the United States as the local governing authority (R. 13-18). With statehood, the basis of federal—and CAB—jurisdiction changed. The federal government surrendered its local guardianship by admitting Hawaii to the Federal Union "on an equal footing with the other states in all respects whatever."¹⁸ Hawaii then became the master of its local affairs and the guardian of its local interests—subject, in aviation matters, to the federal reservation of a highly technical jurisdiction resulting from the geographic accident of Hawaii's archipelagic design. As the CAB has observed in its own decisions (R. 13-16), Hawaii's geography is meaningful primarily as the cause of Hawaii's local dependence on air transport. The Hawaii legislature has also emphasized to the CAB in this case the local importance of such transportation to the Hawaiian community and the failure of

¹⁸ Hawaiian Statehood Act, § 1, Pub. Law 86-3, 73 Stat. 4.

existing airlines to meet the community need for "low cost, frill-free" service (R. 30-35). It has also emphasized Hawaii's need, as a state, to provide for such service "on a footing of practical equality with the other states so far as its relations to the federal government in the aeronautical field are concerned at least to the extent that a classification of purely intrastate nonfederal public air carriers may be established by virtue of state authority" (R. 33).

We can think of no questions of fact or law more clearly related to the public interest than those which bear on the relationship between the states and the United States. The problem of state-federal relationships, conflicts and adjustments is high on the list of topics which have absorbed the Supreme Court's attention since the formation of the Union. *Gibbons v. Ogden*, 22 U.S. 1 (1824); *Leiter Minerals v. United States*, 352 U.S. 220, 223 (1957); *Sears Roebuck Co. v. Stiffel Co.*, 376 U.S. 225, 228 (1964); *United States v. Shimer*, 367 U.S. 374 (1961); *Polar Ice Cream & Creamery Co. v. Andrews*, 375 U.S. 361, 373 (1964). Moreover, the Court has admonished that "in ascertaining the scope of congressional legislation a due regard for a proper adjustment of the local and national interests in our federal scheme must always be in the background" *Federal Trade Commission v. Bunte Bros.*, 312 U.S. 349, 351 (1941). In *Palmer v. Massachusetts*, 308 U.S. 79, 84 (1939), the Court said:

"To be sure, in recent years Congress has from time to time exercised authority over purely intrastate activities of an interstate carrier when, in the judgment of Congress, an interstate carrier constituted, as a matter of economic fact, a single organism and could not effectively be regulated as to some of its interstate phases without drawing local business within the regulated sphere. But such absorption of state authority is a delicate exercise of legislative policy in achieving a wise accommodation between the needs of central control and the lively maintenance of local institutions. Therefore in construing legislation, this

court has disfavored in-roads by implication on state authority and resolutely confined restrictions upon the traditional power of states to regulate their local transportation to the plain mandate of Congress."¹⁹

Since the statute which the CAB administers authorizes exemption of carriers in the public interest, the CAB reasonably may be asked to consider whether use of the exempting power should not at least be pondered, relative to intra-Hawaiian transactions, in aid of "the lively maintenance of local institutions." The Board, we contend, committed flagrant error in refusing even passing notice of the state's contention that the public interest called for preservation of local power over local commerce. Hawaii cited to the Board "a strong and unsatisfied demand by the people of this State" for low cost transportation "which the existing carriers have not furnished." It emphasized the "impracticability of all other competitive means of intercity transportation" in Hawaii. It told the Board that "Hawaii alone of all the fifty states is prevented from dealing with this intrastate matter" in the absence of exemption. These are formidable matters "of primary and pressing concern to the State of Hawaii" (R. 33). We submit that when a state charges suffocation by the Board of a state power which the state needs for its well-being and which all other states possess, the minimum acceptable response is an examination of the facts—rather than a sullen refusal even to ponder the state's necessity, or a bland explication that carriers which have never proved their virtue must be sheltered from competition in every event.

The courts have long insisted that state police powers be treated with federal deference. In *Sinnott v. Davenport*, 63 U.S. 227, 243 (1859), the Court said:

"We agree, that in the application of this principle of supremacy of an act of Congress in a case where

¹⁹ To like effect see *Davies Warehouse Co. v. Bowles*, 321 U.S. 144, 154 (1944).

the state law is but an exercise of a reserved power, the repugnance or conflict should be direct and positive, so that the two acts could not be reconciled or consistently stand together . . .”²⁰

“[J]udicial deference to state action requires, whenever possible, that a state not be thwarted in its policy.” *Tank Truck Rentals v. Commissioner*, 356 U.S. 30, 35 (1958). “It should never be held that Congress intends to supersede, or by its legislation suspend, the exercise of the police powers of the states, even when it may do so, unless its purpose to effect that result is clearly manifested.” *Reid v. Colorado*, 187 U.S. 137, 149 (1903); *Kelly v. State of Washington*, 302 U.S. 1, 11 (1937). See also *Missouri Pacific R. Co. v. Norwood*, 283 U.S. 249, 256 (1931); *Brotherhood of Locomotive Engineers v. Chicago, R. I. & P. R.R. Co.*, — U.S. —, 34 L.W. 4103, 4104 (1966).

A solid body of authority thus establishes that powers inherent in state government merit Congressional respect and forbearance. The same body of authority shows that federal courts establish no facile presumptions in favor of the extinction of state powers by cavalier measures of federal supersession.

If the Federal Aviation Act contained no exemption authority, we would have to concede, at least as a matter of construction, that it superseded Hawaii’s police power over its internal commerce. Since it *does* contain exemption provisions, no such supersession need be inferred—or should be. To apply § 416(b) grudgingly or narrowly is to flout the *Tank Truck* mandate that “whenever possible . . . a state not be thwarted in its policy.”

²⁰ Quoted and followed in *Kelly v. State of Washington*, 302 U.S. 1, 10 (1937).

**(c) The Commerce Involved and the Policy of the
Federal Aviation Act**

This Court's decision in *Island Airlines v. C.A.B.*, 352 F. 2d 735 (1965), perhaps forecloses any contention that Hawaiian interisland commerce is not interstate commerce in the technical sense for purposes of federal jurisdiction if the federal government insists on exercising such jurisdiction.²¹ It does not in any sense foreclose inquiry as to whether the federal government does so insist, or should. That it does not so insist is established by the inclusion of exemptive authority in the Act. That it should not so insist is established by the broad policies of the Act itself, considered in the light of the power-distribution scheme of the federal Constitution.

Under the Constitution (Art. 1, § 8), the Congress has power to regulate commerce "with foreign Nations, and among the several States, and with the Indian Tribes." The states were at an early date excluded from any regulation of such commerce which conflicted with the constitutional grant to the federal government, or with federal laws enacted thereunder. *Gibbons v. Ogden*, 22 U.S. 1 (1824). But state powers over commerce—including interstate and foreign—exercisable without impairment of the federal grant, were rigorously protected. *Cooley v. Board of Wardens*, 53 U.S. 299 (1851). The decisions heretofore cited (*supra*, pp. 16-17) show a strong and steady current

²¹ Apparently it is "interstate" under the definition in § 101(20)(a) of the Federal Aviation Act (49 U.S.C. 1301(20)(a)) even though no second state is involved. On the other hand, the voyage from San Francisco to San Diego in *Lord v. Goodall*, 102 U.S. 541, 544 (1881) on which rests whatever jurisdiction the federal government has over intra-Hawaiian commerce between the islands, was held to be a voyage "in commerce with foreign Nations." This raises a perplexing problem because interisland commerce is *not* "foreign air commerce" or foreign air transportation under the definitions of the Federal Aviation Act (§ 101(20)(c), 49 U.S.C. 1301(20)(c), and § 101(21)(c), 49 U.S.C. 1301(21)(c)). If it is not foreign commerce under the Act and not interstate commerce under the Constitution, the basis of federal jurisdiction disappears. We urge this view upon the Court if the jurisdictional issue is still open under *Island Airlines v. C.A.B.*, 352 F. 2d 735.

of reluctance to extinguish state police (i.e., regulatory) powers by presumption or implication of federal supersession.

The Federal Aviation Act incorporates a regulatory design which in all respects emphasizes its concern with interstate and foreign commerce and with the promotion and regulation of a national and international—as distinguished from local—aviation industry. Thus, § 101 (10) (49 U.S.C. 1301 (10)) defines air transportation as meaning “interstate, overseas, or foreign” air transportation “or the transportation of mail by aircraft.” Interstate air transportation is defined in § 101 (21) (49 U.S.C. 1301 (21)) as transportation in commerce between places in different states, or within U. S. territories or the District of Columbia, and—

“between places in the same State of the United States through the airspace over any place outside thereof.”

The same subsection defines overseas air transportation as carriage in commerce between the U. S. mainland and its territories or between territories; and defines foreign air transportation as carriage in commerce between the United States and places outside thereof.

Every detail of this definitional pattern relates to interstate or international or intraterritorial commerce except the indented quotation extending the “interstate” definition to flights between places in the same state through airspace over a place outside. When the present Act was passed in 1958 (and its predecessor Act in 1938), Hawaii had not become a state. The country was a solid composite of contiguous states and the provision relative to flights between places in a state through a place outside described for every practical purpose a genuine interstate situation—e.g., a flight starting in state A, traversing state B, and ending in state A. No state then in the Union presented the problem which confronts Hawaii of *neces-*

sitating flight beyond its borders in order to complete an intrastate movement of substantial state importance. Consequently the Congress could hardly have considered that it was legislating out of existence any state's power over its intrastate air commerce.

Aside from the matter of definition, the Act as a whole is incompatible with any such parochial application as the CAB has here attempted. Section 102 (49 U.S.C. § 1302) sets forth a declaration of policy for the Board, listing matters which the Board is to consider as in the public convenience and necessity. These include the encouragement and development of an air transportation system adapted to the present and future needs of "the foreign and domestic commerce of the United States, of the Postal Service, and of the National defense"; the assurance of safety and fostering of sound economics in "such transportation"; competition necessary to sound development "of an air-transportation system properly adapted to the needs of the foreign and domestic commerce of the United States, of the Postal Service, and of the national defense." Section 401 (49 U.S.C. 1371) provides for issuance of certificates to engage in air transportation on the basis of public convenience and necessity (as thus spelled out). Section 406(b), 49 U.S.C. 1376(b), permits mail pay scaled to promote service "of the character and quality required for the commerce of the United States, the Postal Service, and the national defense."

Section 416, 49 U.S.C. 1386, authorizes the CAB to establish various classifications of air carriers, and to exempt carriers or classes, wholly or in part, from economic regulation if it finds:

- (i) That enforcement would be an undue burden on the carrier (or class) "by reason of the limited extent of, or unusual circumstances affecting" the carrier or class; and
- (ii) Enforcement is not in the public interest.

These provisions collectively show that the Act was not designed to regulate the local and isolated service proposed by Island under state auspices and solely between places in a state constituting a detached community thousands of miles from the U. S. mainland. The service proposed by Island is not geared into "the foreign and domestic commerce of the United States" since it will serve only the local commerce of Hawaii. It is not geared into the Postal Service because it will carry no mail. It is not geared into the defense establishment because it is planned merely as a civilian service, not coordinated with any military function. It is, in short, not a part of the national air transportation system to which the mandate of the CAB is directed and limited. Even a proposal for direct service between the U. S. mainland and the outer Hawaiian islands was disapproved by the CAB because it did not fit into the agency's "system" concept. *Hawaiian Common Fares Case*, 10 C.A.B. 921 (1949). (R. 17).

Island's is not the only service which differs from those which the Act was meant to regulate; so, too, since statehood, do those of Hawaiian and Aloha. Neither (as we have noted above) has proved, under the conditions of Hawaiian statehood, a case of public convenience and necessity; quite possibly neither could. Nevertheless, both have been covered with an impenetrable blanket of competitive immunity on grounds of an earlier public interest which the CAB has never reviewed since the change in Hawaii's status and which now is exclusively Hawaii's function to determine.

That the Act contemplates a residuum of state control over aviation is indicated by section 204 (b) (49 U.S.C. 1324 (b)) which provides for CAB cooperation (including joint hearings) with state agencies "in connection with any matter arising under this Act within its jurisdiction, and to avail itself of the cooperation . . . of such State agencies as fully as may be practicable . . ." Instead

of cooperating with Hawaii in a matter of vital State concern, the CAB proceeded in cynical defiance of the state, first by securing an injunction against the carrier whose operation the state had authorized, and thereafter by disregarding the state's exemption petitions attesting its urgent local needs.

The Board's ultimate findings—all in conclusory form following the statutory language—were that Island had failed to show (i) that enforcement of the Act would be an undue burden due to the limited extent of Island's operations or unusual circumstances affecting them; and (ii) that enforcement would not be in the public interest. It was wrong on all aspects of both conclusions.

We claim that the burden of a certification proceeding is undue if the proceeding is foredoomed because the Act does not cover the service described. That, we submit, is the present case. Island is not proposing a service susceptible to integration into a national air transportation system. It is not proposing to engage in the foreign or domestic commerce of the United States but in the local commerce of the State of Hawaii. It will not carry mail (and is not authorized to do so), nor has it any national defense attributes. If the service is not within the Board's authority to certify, it is not within the Board's authority to exclude, and any obligatory proceeding to invoke Board action beyond its powers would be an undue burden.

Not only would the burden of a certification case be inherently undue; it would be so on account of the limited extent of the Island service proposed and the unusual circumstances affecting it. The limited extent—including the isolated locale—of the service has been discussed above. "Unusual circumstances" are abundantly present in the geography of Hawaii and its constitutional consequences—both of which are not only unusual but unique—and so characterized by the committee which reported the Hawaii statehood bill (R. 53). The CAB in refusing to detect

unusualness of circumstance in a situation which lacks a counterpart in the Board's regulatory universe is setting an unattainable standard of unusuality.

(d) The Federal Fisc

While the rationale of the order under review is sub-luminous, the provisions emphasizing the extent of past subsidies to Hawaiian and Aloha and their prospect of future losses imply that the CAB purported to act in the role of fiscal guardian to the federal government. More specifically, the CAB seemed to be annulling Hawaii's power to regulate its internal commerce because such annulment would make life cheaper for the federal government.²² We contend that Island's right to engage in intra-Hawaiian commerce and Hawaii's right to regulate such commerce are not exterminable for that reason.

Penn Dairies v. Milk Control Commission, 318 U.S. 261 (1943), held in particular that Pennsylvania's commission-fixed minimum prices for milk were applicable to purchases in the state by the federal government; and held in general that state regulatory power is not curtailed or extinguished because it increases the federal government's cost of doing business. Among the Court's quotable pronouncements are the following (318 U.S. at 269, 270-71, 275):

“ . . . the mere fact that non-discriminatory taxation or regulation of the contractor imposes an increased economic burden on the government is no longer regarded as bringing the contractor within any implied immunity of the government from state taxation or regulation.”

* * *

²² The Board could have reasoned that: (a) past subsidy would look prodigal if its beneficiaries were not perpetuated; (b) federal loan guarantees for Hawaiian and Aloha might have to be met if those carriers should fail; (c) future losses would have to be offset by future subsidies. Only by a blind attribution to the Board of some such reasoning process can any relationship be detected between the Board's conclusions and its unrevealed concept of public interest.

"We have recognized that the Constitution presupposes the continued existence of the states functioning in coordination with the national government, with authority in the states to lay taxes and to regulate their internal affairs and policy, and that state regulation like state taxation inevitably imposes some burdens on the national government of the same kind as those imposed on citizens of the United States within the state's borders, see *Metcalf & Eddy v. Mitchell*, *supra*, 269 U.S. at pages 523, 524, 46 S. Ct. at page 174, 70 L. Ed. 384. And we have held that those burdens, save as Congress may act to remove them, are to be regarded as the normal incidents of the operation within the same territory of a dual system of government, and that no immunity of the national government from such burdens is to be implied from the Constitution which established the system, see *Graves v. People of the State of New York ex rel. O'Keefe*, 306 U.S. 466, 483, 487, 59 S. Ct. 595, 599, 601, 86 L. Ed. 927, 120 A.I.R. 1466."

* * *

"Considerations which lead us not to favor repeal of statutes by implication [citations] should be at least as persuasive when the question is one of the nullification of state power by Congressional legislation."

* * *

"Furthermore we should be slow to strike down legislation which the state concededly had power to enact, because of its asserted burden on the federal government. For the state is powerless to remove the ill effects of our decision, while the national government, which has the ultimate power, remains free to remove the burden."

In *Penn Dairies*, the state regulation impinged directly on the cost of federal procurement. The federal government had no choice but to pay the regulated price if it bought any Pennsylvania milk. Nevertheless the Court spoke (and ruled) strongly against invalidation of state regulation unless it discriminates against a federal activity or conflicts with a federal law. In the present case, Hawaii has taken no action which directly affects any cost of any

federal activity, and none which could do so even indirectly unless the federal government voluntarily should choose to react by escalating its activities as salvor of the two existing (and ailing) airlines in the event their revenues should suffer from Island's competition—a prospect which we contest for reasons hereafter noted.

(e) Exemption Precedents—CAB

Two CAB exemption actions—the *Catalina Island Service Investigation*, Order No. E-19678 (1963), and *Application of Starflite Inc.*, Order No. E-21535 (1964)—offering relevantly close parallels to the present application are discussed in the Island petition (R. 24-25). The *Starflite* application, terminating in CAB order No. E-21535, offers particularly strong support for the relief sought by Island. In that case the applicant had been conducting an intrastate operation between East Hampton, Long Island and La Guardia Airport. Service had been performed on a regular basis with DC-3 aircraft but was confined to weather conditions governed by visual flight regulations. The reason for this restriction was that instrument traffic patterns into La Guardia would require the carrier to fly outside the confines of the State of New York and thereby force it to engage in interstate air commerce. The CAB granted the exemption sought by *Starflite* stating in part:

“The authority sought is extremely limited, covering only flights between points situated in the same state which occasionally, because of weather conditions, involve navigation over air space outside of the state. Grant of exemption herein will not permit the carrier to expand the geographic area it may already serve on intrastate operations; it will, however, enable the carrier to use alternate IFR routings when VFR operations are not permissible. Under the circumstances, we find that grant of the exemption sought is in the public interest.

In reaching its conclusion the Board has taken into account, as considerations which warrant use of its

exemption power, the limited nature of the authority granted herein, the relatively small size and restricted nature of the applicant's operations, and the unusual flight pattern situation necessitating an exemption in this instance. To require a certification proceeding in order to conduct the proposed operations would be disproportionate to the size of the operations, unduly burdensome on the carrier, and not in the public interest."

The only conceivably-pertinent difference between *Starflite* and the Island application was that in the former, "No certificated route carrier is authorized to provide air service between East Hampton and La Guardia; hence it appears that no significant adverse effect upon any other air carrier would result from grant of the exemption"—whereas in Hawaii, there are, as noted, two certificated carriers in intra-Hawaiian commerce, but the CAB conducted no proceedings permitting it to know or to find that Island would hurt them. Further, a potential loss of traffic by either of such carriers cannot be equated with harm to the public interest where their own certificates were issued under superseded conditions (i.e., when Hawaii was a territory) and have never been reexamined in the light of current certification requirements.

Except for the distinction noted, virtually every condition found in *Starflite* and cited in support of exemption is present in this case, and equally merits citation in support of exemption. There, as here, flights were "between points situated in the same state." There, as here, the flights involved "navigation over air space outside of the state."²³ There, as here, "exemption . . . will not permit the carrier to expand the geographic area it may already

²³ *Starflite* was forced outside the state by meteorology; Island by geography. What is the legal distinction? *Starflite*'s use of outside air space was occasional (depending on the frequency of bad weather); Island must always use outside air space. Again, what is the legal distinction? In what respect is the interest of the U.S. in interstate commerce differently affected because a carrier uses outside air space for convenience rather than through necessity?

serve on intrastate operations.” There, as here, the applicant’s service was of “relatively small and restricted nature.” There, as here, the service involved an “unusual flight plan situation necessitating an exemption.” There, as here, the burden of certification proceedings “would be disproportionate to the size of the operations, unduly burdensome on the carrier, and not in the public interest.”

In *Starflite*, each of the enumerated conditions pointed towards exemption. In *Island*, the equivalent conditions were held to point the other way. The difference is unexplainable except as a manifestation of pure caprice.

(f) An Exemption Precedent—ICC

In *Motor Carrier Operation in the State of Hawaii* (Ex Parte No. MC-59, 1960), 84 M.C.C. 5, the Interstate Commerce Commission considered whether to exempt the operations in Hawaii, after statehood, of motor carriers engaged in interstate or foreign commerce. The applicable provision of the Interstate Commerce Act was section 204(a)(4a) (49 U.S.C. 304(a)(4a)), which requires the ICC—

“To determine * * * whether the transportation in interstate or foreign commerce performed by any motor carrier or class of motor carriers lawfully engaged in operation solely within a single State is in fact of such nature, character, or quantity as not substantially to affect or impair uniform regulation by the Commission of transportation by motor carriers engaged in interstate or foreign commerce in effectuating the national transportation policy declared in this Act. Upon so finding, the Commission shall issue a certificate of exemption to such motor carrier or class of motor carriers . . .”

The procedure followed by the ICC in passing on the question of exemption was in notable contrast to the procedure—or absence of procedure—of the CAB in this case. As described by the ICC (84 MCC at 6):

“ . . . we instituted the instant proceeding in order to develop an adequate record to determine [the statutory issues] . . . Our order provided an opportunity for all interested parties to be heard at oral hearings at Honolulu, Hawaii, and Washington, D. C., and also permitted the filing of written statements of data, views, and arguments respecting these matters.”

The report then describes the hearings and recites the receipt of briefs, statements of fact and argument, all of which are then examined in a printed opinion covering 28 closely printed pages. Upon this exhaustive review, the Commission determined to grant a blanket exemption. The following quotation represents a summary of the agency's reasoning:

“The situation with respect to Hawaii is unique. Unlike other States it does not border on any State or foreign country; indeed, its shores are more than 2,000 miles from the mainland. Even Alaska, with which Hawaii is sometimes compared regarding transport regulation, has a highway connection with the other continental States and Canada over which motor-carrier operations take place; additionally, almost all water traffic in the Alaska trade is transported by carriers operating solely between Alaska and the other Pacific Coast States, whereas much of the water transportation between the mainland and Hawaii is by water carriers also engaged in foreign commerce. Apart from its physical isolation from the mainland and the remoteness of most of its motor carriers from the operations of other carriers subject to our jurisdiction, Hawaii's component parts are separated by expanses of water ranging from 25 to 70 miles in width, and its terrain is extremely mountainous in character, geographical features which necessarily limit motor transportation to relatively short distances. Additionally, nearly 80 percent of the population of Hawaii is concentrated in one incorporated community over whose docks the greater portion of the interstate traffic moves, and because of our lack of jurisdiction over water carriers operating between the continental States and Hawaii, we are without authority to approve the

establishment of through routes and joint rates between such water carriers and the motor carriers operating in Hawaii or on the mainland.

Considering all factors, we are persuaded that the exercise of our jurisdiction in the regulation of Hawaiian motor carriers, whose operations in large part might well be characterized as in the nature of pickup and delivery (particularly as to inbound traffic, a large portion of which comes to rest at the ports), would amount to unwarranted Federal regulation of a stub ended, essentially local, operation for no useful purpose."

The question for the ICC was substantially similar to that of the CAB here. In each instance, the basic question was whether small and essentially local transport operations in a state isolated by over 2,000 miles from the U. S. mainland were so far integrated into a national pattern of interstate or foreign commerce as to call for coordinated regulation under a federal master plan. The ICC said no, on the basis of searching investigation and meticulous fact-finding. The CAB said yes, on the basis of no investigation, no fact-finding, and obdurate refusal to consider the matters submitted to it. The ICC method was right; the CAB wrong. The principal difference between *Ex Parte MC-59* and this case is that the commerce covered by the ICC exemption was clearly *interstate* commerce in the true sense of commerce moving between one state and another; whereas the commerce covered by the CAB refusal of exemption is purely commerce moving between places in the same state.

B. DENIAL OF EXEMPTION DEPRIVES THE STATE OF HAWAII OF "EQUAL FOOTING" IN THE FEDERAL UNION

The Hawaiian Statehood Act, Pub. Law 86-3, (73 Stat. 4) admitted Hawaii "into the Union on an equal footing with the other States in all respects whatever . . ." (§ 1). The Act provided (§ 15) that any territorial law enacted by the Congress—i.e., a law whose validity depended on

congressional authority to govern Hawaii as a territory—should remain in force for two years after admission, or until Hawaii should amend or repeal it.

The act admitting Alaska as a state contained equivalent provisions. They came before a three-judge district court in *Interior Airways v. Wien Alaska Airlines*, 188 F. Supp. 107 (D.C. Alaska, 1960), in an injunction suit to restrain Wien from prosecuting and the CAB from entertaining a complaint proceeding against Interior, covering activities during the two-year period when various federal statutes continued in effect as “territorial laws.” The suit rested on the contention that Interior was engaged only in intrastate commerce in Alaska and that the CAB therefore lacked jurisdiction. Interior claimed, on the basis of *Coyle v. Smith*, 221 U.S. 559 (1911), that federal regulation of its intrastate activity would deprive Alaska of control over its intrastate commerce in violation of the equal-footing provision of the Alaska statehood act. The Interior contention was rejected—but solely on the ground that the CAB was asserting jurisdiction during the two-year interval in which the Federal Aviation Act remained in force by choice of Alaska itself, which could have superseded the Act at any time by passing its own aviation statute. The Court treated Alaska’s purposeful non-adoption of a superseding law as an adoption by the state of federal law for the transitional period, and concluded that this involved no impairment of Alaskan sovereignty. The opinion contains the following observations:

“There is no question but that the authority for the regulation of intrastate air commerce by the Civil Aeronautics Board is authorized, if at all, solely by such ‘Territorial laws.’ We hold that Sec. 401(a) of the Federal Aviation Act of 1958 is such a law.” (188 F. Supp. at 111)

* * *

“We cannot read *Coyle* as dispositive of the issue. We agree that under *Coyle*, and under the cases discussed

in some detail therein, as well as those cases since determined by the Supreme Court, no state can be deprived of any 'attributes of power essential to its equality with other states.' The essence of the power of statehood must be maintained without impairment by any condition of admission, compact, or agreement. A state cannot be restricted in its legislative power in respect of any matter which is not plainly within the regulatory power of the national government. 'Each state must be competent to exercise that residuum of sovereignty not delegated to the United States by the constitution.' What is prohibited is not *all* conditions, compacts, or stipulations, but only those which would not be valid and effectual if the subject of Congressional legislation after the state's admission.

Here we find no deprivation of any of Alaska's power. She could and can terminate the regulation of intrastate air commerce by the Federal Government at any time she chooses to act." (188 F. Supp. at 112)

The case thus turned on a matter of timing—i.e., the exertion of CAB power during the transitional period when territorial laws remained in force by the state's decision. The clear portent is that if the CAB had tried to flex its intrastate muscles *after* the transition, it would have infringed Alaska's equal footing as expounded in *Coyle v. Smith*.

That case held that under the equal footing provision of the Oklahoma admission act, the state could establish its capital in any location of its choice despite a provision in the act that the capital be at Guthrie until a date specified. The opinion contained the following presently-relevant pronouncements:

"So far as this court has found occasion to advert to the effect of enabling acts as affirmative legislation affecting the power of new states after admission, there is to be found no sanction for the contention that any state may be deprived of any of the power constitutionally possessed by other states, as states, by

reason of the terms in which the act admitting them to the Union have been framed.” (221 at 570)

* * *

“The plain deduction from this case [*Pollard v. Hagan*, 3 How. 212] is that when a new state is admitted into the Union, it is so admitted with all of the powers of sovereignty and jurisdiction which pertain to the original states, and that such powers may not be constitutionally diminished, impaired, or shorn away by any conditions, compacts, or stipulations embraced in the act under which the new state came into the Union, which would not be valid and effectual if the subject of congressional legislation after admission.” (221 U.S. at 573)

* * *

“It may well happen that Congress should embrace in an enactment introducing a new state into the Union legislation intended as a regulation of commerce among the states, or with Indian tribes situated within the limits of such new state, or regulations touching the sole care and disposition of the public lands or reservations therein, which might be upheld as legislation within the sphere of the plain power of Congress. But in every such case such legislation would derive its force not from any agreement or compact with the proposed new state, nor by reason of its acceptance of such enactment as a term of admission, but solely because the power of Congress extended to the subject, and therefore would not operate to restrict the state’s legislative power in respect of any matter which was not plainly within the regulating power of Congress.” (221 U.S. 574)

The CAB position (R. 168(a) - 168(b)) is that the Congress, “in enacting the Hawaiian Statehood Bill . . . fully considered the regulatory problem and determined that because of the geographic situation, Federal regulation of the interisland air transportation should continue. This Congressional determination is dispositive of Island’s contention.”

We understand this to mean that the committee comments on the admission bill (see pp. 8-9, *supra*) are to be taken as grafts on the admission legislation itself, having the effect of exterminating Hawaii's control of its intra-Hawaii air commerce because of the state's insular physical structure. The Board could hardly make a clearer case in derogation of the new state's equal footing, or one more pointedly at odds with *Coyle v. Smith*.

We make no claim that the Federal Aviation Act is in all circumstances unconstitutional as applied to Hawaiian interisland commerce, but note that "a law which is constitutional as applied in one manner may . . . violate the constitution when applied in another," *Alabama State Federation of Labor v. McAdory*, 325 U.S. 450, 462 (1945); and that "the constitutionality of a statute, valid on its face, may be assailed by proof of facts tending to show that the statute as applied to a particular article is without support in reason because the article, although within the prohibited class, is so different from others of the class as to be without the reason for the prohibition." *United States v. Carolene Products Co.*, 304 U.S. 144, 153 (1938).

The CAB has here applied the Federal Aviation Act not to an "article" but to a situation "so different from others of the class as to be without the reason" of the statute's regulatory scheme. Hawaii's situation reaches the ultimate extreme of difference from others to which the Act has been applied. The Board's unduplicated and unduplicable effort to regulate pure intra-Hawaii commerce not only stretches the commerce clause beyond its stretchable limit but negates Hawaii's—and only Hawaii's—position as an equal among equals. For that reason in addition to many others, the Board's action must be annulled.

C. THE BOARD'S PROCEDURE WAS UNLAWFUL AND ITS FINDINGS UNSUPPORTED

The CAB did not deny the petition for legal insufficiency of its own allegations. It received answering pleadings (R. 38-157) from the interveners which contested the petition and alleged new facts. Without affording any procedure for testing either the truth or legal sufficiency of the answers, the Board summarily denied (1) the Island petition; and (on the basis of such denial) (2) the supporting state and county petitions—in reliance on material alleged in the answers and uncritically accepted as true, without proof. This was error, involving a denial of constitutional due process and a failure to find the requisite facts. It was also prejudicial error because Island would have contested the material facts as alleged by interveners and the contest would have been more than formal. A single illustration will suffice.

The CAB found (R. 168(a)), on unsupported estimates based only on the *ipse dixit* of the interveners (whose estimates were themselves inconsistent) that Aloha would lose \$1,000,000, and Aloha plus Hawaiian \$4,856,000, in annual revenue to Island's lower-cost service. This finding was made in October, 1965.

Island would have shown, if permitted to do so, that in August, 1965 the Board published a staff study on "Traffic, Fares and Competition, Los Angeles-San Francisco Air Corridor"²⁴ which refutes dramatically the Board's finding here that low-fare competition diverts traffic and revenue without expanding either. We request the Court to notice this study officially.

²⁴ Staff Research Report No. 4, Research and Statistics Division, Bureau of Accounts and Statistics, Civil Aeronautics Board, August, 1965. This study (less appendix) is annexed to this brief as Appendix B.

The focus of the Los Angeles-San Francisco study was the effect on that market of Pacific Southwest Airlines (PSA) of which the study states (p. 7):

“A small intra-state carrier, Pacific Southwest Airlines, started service in 1949 with a single, rented DC-3. Always a very low-fare carrier, and operating up and down the coast between San Diego, Los Angeles, and San Francisco, PSA was once called ‘The Poor Sailor’s Airline’.”

In other words, PSA was the California intrastate equivalent of Island.

The result of PSA’s entry into the service on a low-cost basis is summarized thus:

“With lower fares, PSA forged ahead in volume of traffic. But starting in 1962, the trunk airlines’ determined competition in both quality of service and fares has brought them, together, equal with PSA in number of coach passengers. *And these competitive efforts have, undoubtedly, expanded total traffic far above what it might otherwise be.*” (p. 11; italics ours.)

“PSA has thus appealed, successfully, to the large potential market—people who formerly traveled by other modes or did not travel at all.” (p. 13.)²⁵

“Pacific Southwest Airlines’ always-low fares have attracted traffic from competitors, have induced fare reductions by them, have brought down average fares and have apparently expanded total traffic far above with it might otherwise be.” (p. 21.)

“Since the market is price-elastic, further declines in fares would produce additional gross revenues for the carriers.” (p. 23.)

Clearly, the functionaries who wrote the CAB order in the present case had never heard of the study. Since it invalidates the Board’s basic factual assumption and the

²⁵ This is a convincing answer to the assertion (R. 61) that Hawaii and Aloha cannot grow significantly because they now have all the existing traffic.

reason for making it, it is a critical item of proof and the Board could not lawfully foreclose Island from submitting it and arguing its meaning.²⁶

Section 416(b) does not provide for a hearing on exemption applications, and it has been held that a "full" hearing is not required. *Eastern Airlines, Inc. v. Civil Aeronautics Board*, 185 F. 2d 426 (D.C. Cir. 1950), vacated as moot 341 U.S. 901. The case invites these observations:

1. The plaintiff was not the applicant for exemption but the applicant's competitor. A competitor's demand for a hearing raises merely a question of the competitor's standing. (185 F. 2d at 429)
2. Even so, the court said that a decision based on an *arbitrary* finding or belief "might not be enough and some proceedings may be necessary." (185 F. 2d at 428) It then noted that "In this case there were proceedings, in the course of which several verified documents were filed with the Board." (185 F. 2d at 428; see also note 4) *No such proceedings were had before the Board in Island.*
3. The court noted that even where no act of Congress requires a hearing, "the Administrative Procedure Act must be followed where a hearing is necessary

²⁶ The PSA case has an interesting and relevant history. The Board while now citing PSA pridefully to prove the virtue of low rates, says nothing of early Board efforts to kill it off. The truth is that the CAB tried to drive PSA from the California skies in an attack paralleling its present campaign against Island. The jurisdictional basis for the suit against PSA was that some of its passengers came from or continued to places outside of California even though PSA stayed inside. A district court refused an injunction on the ground that the out-of-state passengers did not convert PSA service into interstate air transportation. *Civil Aeronautics Board v. Friedkin Aeronautics, Inc.* (S.D. Calif., 1954), 4 Avi. 17,457. This court reversed the decision and remanded it to the district court, *Civil Aeronautics Board v. Friedkin Aeronautics*, 246 F. 2d 173 (1957), to make requisite findings of fact as to the conditions of ticketing and handling out-of-state passengers. The CAB then dropped the case and PSA has operated to the present instant without molestation—and also without a CAB certificate or exemption order.

to the protection of constitutional rights.” (185 F. 2d at 428-29) But it then ruled that such a hearing was not available to a competitor—clearly implying that it is available to an applicant.

Cook Cleland Catalina Airways v. Civil Aeronautics Board, 195 F. 2d 206 (D.C. Cir., 1952), held that even an applicant was not there entitled to a hearing; it noted, however (195 F. 2d at 207):

“The Board stated that it would consider as true and accurate all of the allegations of fact in the petition for reconsideration and in the original application.”

The Board made no such statement here, nor could it have. It plainly rejected facts in the petition, accepted facts alleged but not proved by the opposition, and made such unproved facts the basis of decision. A further distinction between this case and *Cook Cleland* is that there the applicant had been given a chance to argue its case orally to the CAB and failed to do so.

We believe that a sound statement of current law on the right to a hearing at the administrative level in the absence of statutory provision therefor is found in the court's opinion in *First Nat. Bank of Smithfield, N. C. v. First Nat. Bank of E. N. C.*, 232 F. Supp. 725 (E.D.N.C., 1964). The case involved the obligation of the Comptroller of the Currency to afford a hearing on applications for branch-banking permits. The Court held that such obligation existed:

“If the use of the word ‘approval’ is deemed to commit agency action to agency discretion within the meaning of the second exception to § 10, nevertheless it must be a sound discretion exercised in a manner that is not violative of procedural due process.” (232 F. Supp. at 729-30)

* * *

“Granting the Comptroller of the Currency a specialized knowledge in the field of banks and banking

and that his decisions should stand if supported by substantial evidence and do not exceed his statutory authority, nevertheless, where, as here, there was no hearing, no record of the proceedings and no findings of fact, but only a bare decision, it cannot be determined whether his acts were arbitrary or illegal." (232 F. Supp. at 730)

* * *

"Any provision of the National Banking Act that would deny procedural due process would raise a serious constitutional question. Considering the legislative history of the Administrative Procedure Act and the intent of Congress in its enactment, the Act is sufficiently elastic to provide procedural due process in the administration of the National Banking Act." (232 F. Supp. at 731)

Procedural due process—or any process—was denied by the CAB in this case, and its order of denial must be set aside.

CONCLUSION

We request that this Court set aside the order under review and direct the CAB to issue an order exempting Island; or alternatively, that the case be remanded for processing under prescribed guidelines and constitutional procedures.

Respectfully submitted,

GEORGE F. GALLAND

G. NATHAN CALKINS

AMY SCUPI

GALLAND, KHARASCH, CALKINS
& LIPPMAN

1824 R Street, N.W.

Washington, D. C. 20009

Attorneys for Petitioner

February 23, 1966

APPENDIX A

Federal Aviation Act of 1958

Section 101. 49 U.S.C. 1301:

- (10) "Air transportation" means interstate, overseas, or foreign air transportation or the transportation of mail by aircraft.

* * *

- (18) "Federal airway" means a portion of the navigable airspace of the United States designated by the Administrator as a Federal airway.

* * *

- (21) "Interstate air transportation", "overseas air transportation", and "foreign air transportation", respectively, mean the carriage by aircraft of persons or property as a common carrier for compensation or hire or the carriage of mail by aircraft, in commerce between, respectively—

- (a) a place in any State of the United States, or the District of Columbia, and a place in any other State of the United States, or the District of Columbia; or between places in the same State of the United States through the airspace over any place outside thereof; or between places in the same Territory or possession of the United States, or the District of Columbia;
- (b) a place in any State of the United States, or the District of Columbia, and any place in a Territory or possession of the United States; or between a place in a Territory or possession of the United States, and a place in any other Territory or possession of the United States; and
- (c) a place in the United States and any place outside thereof; whether such commerce moves wholly by aircraft or partly by aircraft and partly by other forms of transportation.

Section 102, 49 U.S.C. 1302:

In the exercise and performance of its powers and duties under this Act, the Board shall consider the following, among other things, as being in the public interest, and in accordance with the public convenience and necessity:

- (a) The encouragement and development of an air-transportation system properly adapted to the present and future needs of the foreign and domestic commerce of the United States, of the Postal Service, and of the national defense;
- (b) The regulation of air transportation in such manner as to recognize and preserve the inherent advantages of, assure the highest degree of safety in, and foster sound economic conditions in, such transportation, and to improve the relations between, and coordinate transportation by, air carriers;
- (c) The promotion of adequate, economical, and efficient service by air carriers at reasonable charges, without unjust discriminations, undue preferences or advantages, or unfair or destructive competitive practices;
- (d) Competition to the extent necessary to assure the sound development of an air-transportation system properly adapted to the needs of the foreign and domestic commerce of the United States, of the Postal Service, and of the national defense;
- (e) The promotion of safety in air commerce; and
- (f) The promotion, encouragement, and development of civil aeronautics.

Section 204, 49 U.S.C. 1324:

* * *

- (b) The Board is empowered to confer with or to hold joint hearings with any State aeronautical agency, or other State agency, in connection with any matter arising under this Act within its jurisdiction, and to avail itself of the cooperation, services, records, and facilities of such State agencies as fully as may be practicable in the administration and enforcement of this Act.

Section 312, 49 U.S.C. 1353:

- (a) The Administrator is directed to make long range plans for and formulate policy with respect to the orderly development and use of the navigable air-space, and the orderly development and location of landing areas, Federal airways, radar installations and all other aids and facilities for air navigation, as will best meet the needs of, and serve the interest of civil aeronautics and national defense, except for those needs of military agencies which are peculiar to air warfare and primarily of military concern.

Section 401, 49 U.S.C. 1371:

- (a) No air carrier shall engage in any air transportation unless there is in force a certificate issued by the Board authorizing such air carrier to engage in such transportation.

* * *

- (d) (1) The Board shall issue a certificate authorizing the whole or any part of the transportation covered by the application, if it finds that the applicant is fit, willing, and able to perform such transportation properly, and to conform to the provisions of this Act and the rules, regulations, and requirements of the Board hereunder, and that such transportation is required by the public convenience and necessity; otherwise such application shall be denied.

Section 406, 49 U.S.C. 1376:

* * *

- (b) In fixing and determining fair and reasonable rates of compensation under this section, the Board, considering the conditions peculiar to transportation by aircraft and to the particular air carrier or class of air carriers, may fix different rates for different air carriers or classes of air carriers, and different classes of service. In determining the rate in each case, the Board shall take into consideration, among other factors, (1) the condition that such air carriers may hold and operate under certificates authorizing the carriage of mail only by providing necessary and adequate facilities and service for the transportation

of mail; (2) such standards respecting the character and quality of service to be rendered by air carriers as may be prescribed by or pursuant to law; and (3) the need of each such air carrier (other than a supplemental air carrier) for compensation for the transportation of mail sufficient to insure the performance of such service, and, together with all other revenue of the air carrier, to enable such air carrier under honest, economical, and efficient management, to maintain and continue the development of air transportation to the extent and of the character and quality required for the commerce of the United States, the Postal Service, and the national defense.

Section 416, 49 U.S.C. 1386:

- (a) The Board may from time to time establish such just and reasonable classifications or groups of air carriers for the purposes of this title as the nature of the services performed by such air carriers shall require; and such just and reasonable rules and regulations, pursuant to and consistent with the provisions of this title, to be observed by each such class or group, as the Board finds necessary in the public interest.
- (b) (1) The Board, from time to time and to the extent necessary, may (except as provided in paragraph (2) of this subsection) exempt from the requirements of this title or any provision thereof, or any rule, regulation, term, condition, or limitation prescribed thereunder, any air carrier or class of air carriers, if it finds that the enforcement of this title or such provision, or such rule, regulation, term, condition, or limitation is or would be an undue burden on such air carrier or class of air carriers by reason of the limited extent of, or unusual circumstances affecting, the operations of such air carrier or class of air carriers and is not in the public interest.
- (2) The Board shall not exempt any air carrier from any provision of subsection (k) of section 401 of this title, except that (A) any air carrier not engaged in scheduled air transportation, and (B), to the extent that the operations of such air carrier are conducted

during daylight hours, any air carrier engaged in scheduled air transportation, may be exempted from the provisions of paragraphs (1) and (2) of such subsection if the Board finds, after notice and hearing, that, by reason of the limited extent of, or unusual circumstances affecting, the operations of any such air carrier, the enforcement of such paragraphs is or would be such an undue burden on such air carrier as to obstruct its development and prevent it from beginning or continuing operations, and that the exemption of such air carrier from such paragraphs would not adversely affect the public interest: *Provided*, That nothing in this subsection shall be deemed to authorize the Board to exempt any air carrier from any requirement of this title, or any provision thereof, or any rule, regulation, term, condition, or limitation prescribed thereunder which provides for maximum flying hours for pilots or co-pilots.

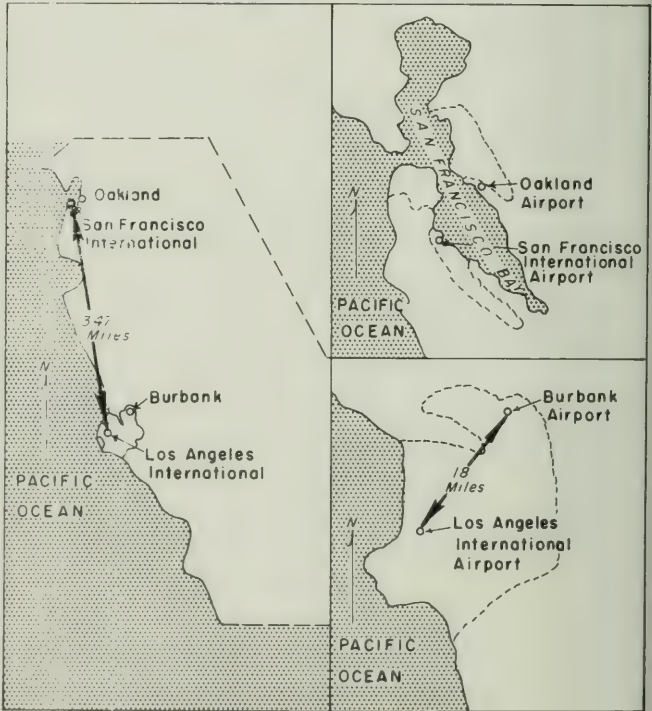


APPENDIX B

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THE LOS ANGELES-BAY AREA AIR TRAVEL CORRIDOR



INTRODUCTION

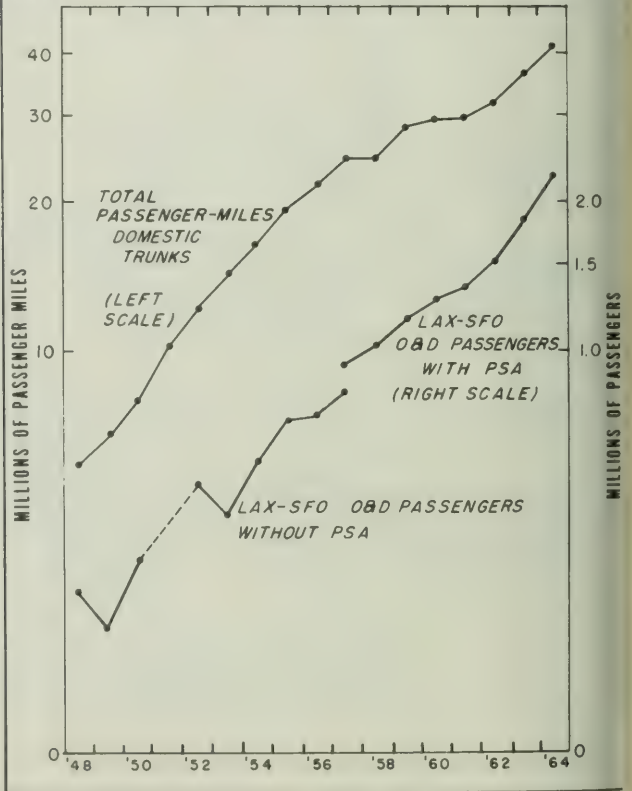
This study of air travel between Los Angeles and San Francisco aims, by interpreting changes in traffic, fares, and other things, to throw light on the factors generating air passenger traffic. The particular focus is the effect of fare changes, since these are subject to some influence by the Civil Aeronautics Board.

The method of study is simple. From the chronology of events in the market, the most significant are selected, their relationships studied, and conclusions drawn according to the best judgment of the investigator. The difficulties are well known, and need only be mentioned here. Historical change is compound of many factors; to isolate and measure them singly is a challenging task.

This is the first of several studies of particular air travel markets, selected because they have been commanding attention by changing fares and burgeoning growth of passenger traffic.

This report was prepared by Messrs. S. Brown, W. Watkins, and K. Paxson and Miss J. Ronson of the Research and Statistics Division of the Bureau of Accounts and Statistics of the Civil Aeronautics Board. The contents of the report are the responsibility of this staff and do not necessarily reflect official views or opinions of the Board Members themselves.

GROWTH OF AIR TRAVEL: TOTAL DOMESTIC MARKET AND LOS ANGELES-SAN FRANCISCO MARKET



DATA: TABLE 1

THE LOS ANGELES-SAN FRANCISCO
AIR TRAVEL CORRIDOR

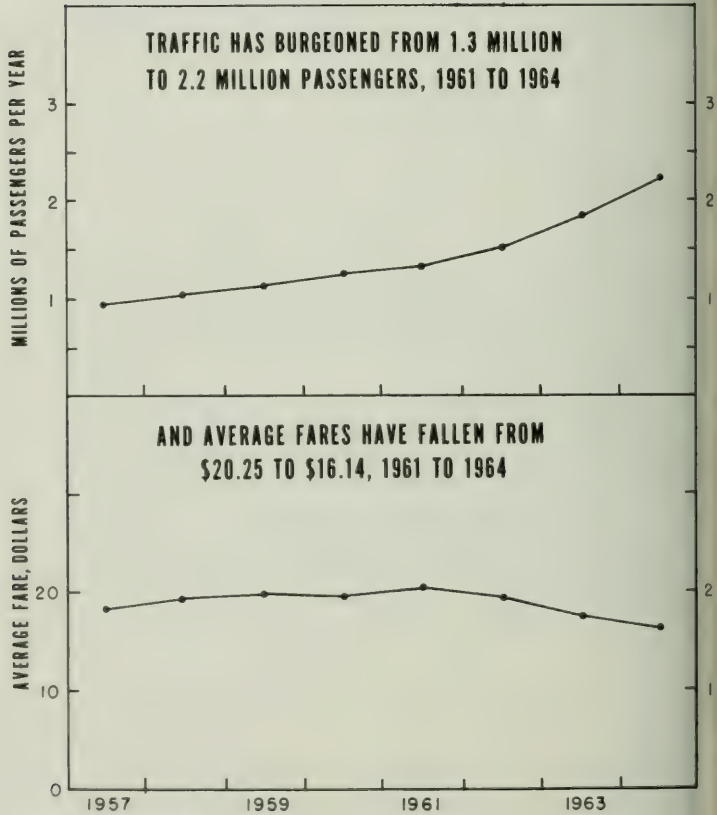
The Market

Los Angeles-San Francisco is the heaviest traveled of all city-pair markets in the world. Air travel on the 347 mile route has grown at a remarkable rate in recent years. From 1957 to 1964 air passengers increased from 940 thousand to 2.2 million, almost 2 1/2-fold. Over the same period for comparison, traffic on the domestic trunk airlines increased 70%, from 24.5 million to 41.7 million passenger-miles.

Part of this vigorous growth is attributable to rapid economic expansion of the West Coast communities. California's population, for example, increased by 27%, 1957 to 1964, compared to a national rate of growth of 12%. Incomes too, are nearly one-fourth higher than the national average and tend to grow at least at comparable rates.

The retardation of growth of air travel from 1957 to 1961, so visible in the national figures, was much less noticeable in the Los Angeles-San Francisco market. Growth since 1961 has accelerated to the phenomenal rate of nearly 19% per year. At 2.2 million in 1964, the number of passengers is expected to be close to 2.7 million in 1965.

ON THE BUSY LOS ANGELES- SAN FRANCISCO ROUTES:



DATA: TABLE 2

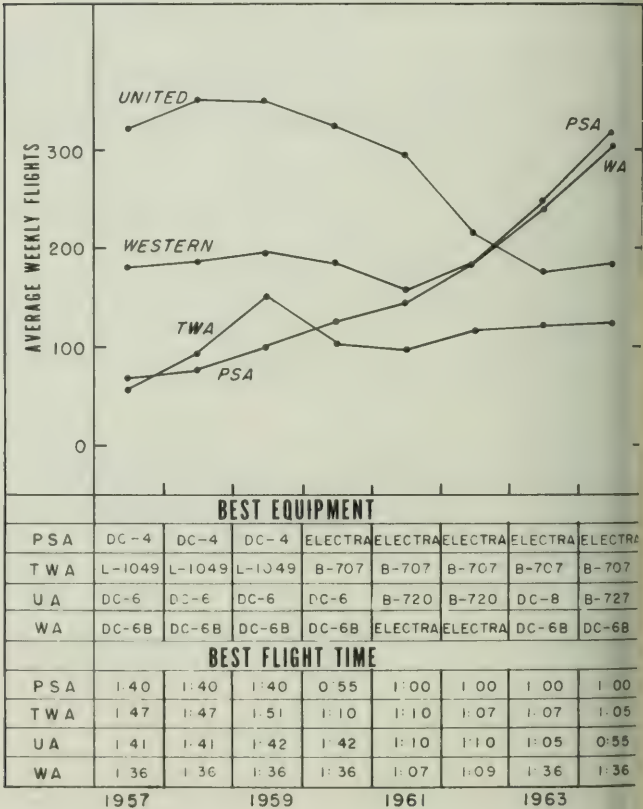
The Growth of Traffic and the Carriers

The chart opposite shows the striking surge, since 1961, of traffic in the Los Angeles-San Francisco air travel market.

At the same time, average fares have dropped more than one-fifth: from more than \$20 for the 347 mile trip, to about \$16 in 1964. From all indications, average fares are declining further this year with continued sharp competition among the carriers. The great surge of traffic accompanying these fare declines suggests that the level of fares may be close to a critical point at which a good deal of diversion from other modes of travel - automobile and bus for example - is taking place. Advertising of the airlines along the Los Angeles to San Francisco highways stresses the low fares, the one-hour flying time, and the greater convenience of air over motor travel.

There are four major air carriers in this market. United Airlines was dominant for years. Western was a close second. Trans-World serves the market only as a segment of longer routes. A small intra-state carrier, Pacific Southwest Airlines, started service in 1949 with a single, rented DC-3. Always a very low-fare carrier, and operating up and down the coast between San Diego, Los Angeles, and San Francisco, PSA was once called "The Poor Sailor's Airline".

FLIGHTS, EQUIPMENT, AND ELAPSED TIME



DATA: APPENDIX B

TRAFFIC, FARES, AND COMPETITION

Flights, Equipment, and Elapsed Time

For the four carriers in the Los Angeles-San Francisco market the chart opposite portrays the trends of their flights, types of aircraft, and scheduled flying times

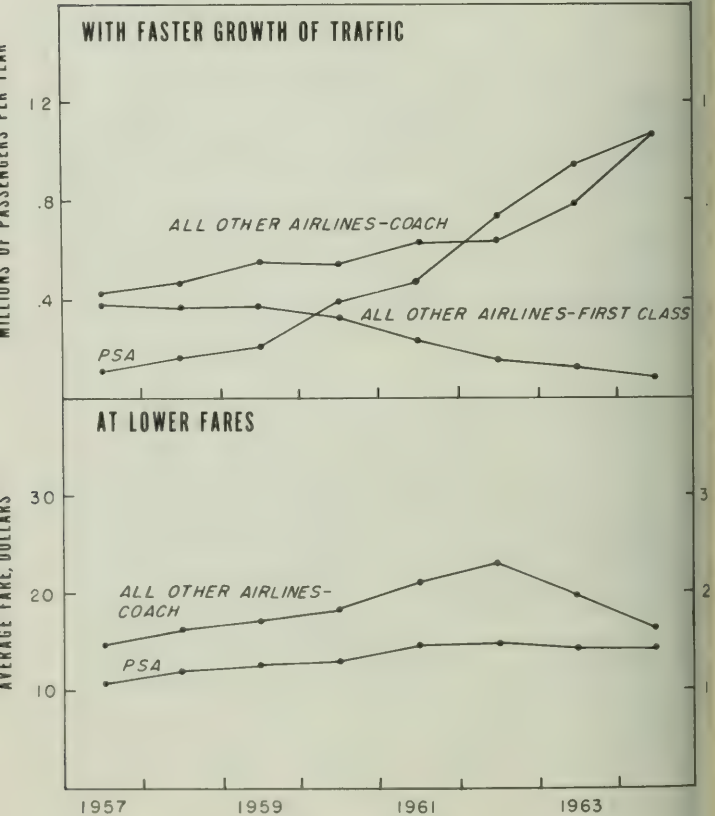
Adding flights in a market may generate traffic for a carrier up to a certain threshold, after that point changes in flights are the effect, not the cause, of changes in traffic. Accordingly, the long run trends of flights offered provide a rough measure of competitive traffic shares - rough because of differences in seats and configuration among the different aircraft types. However, the dramatic change in the relative market positions of the four carriers, 1957-1964 stands out clearly

In these annual figures, PSA's rise has been uninterrupted, and picked up rapidly after 1961. United declined until 1964. Western became a strong contender starting in 1962 with its low-fare, "Thriftyair" service in older DC-6B planes. Trans-World has maintained a fairly steady position

Except for Western's "Thriftyair" experiment, the carriers have since 1960 been fairly competitive with respect to quality of equipment and flying times. PSA was first with Electras in 1960, securing a brief advantage over United and Western in this respect. United first introduced the highly efficient and attractive B-727 in the fall of 1964, stealing a march on all competitors

The changeover from piston to turbine airplane, practically completed by 1961, reduced flying time by about three-quarters of an hour - from an hour and forty minutes to one hour or less.

PACIFIC SOUTHWEST AIRLINES HAS REACHED THE TOP OF THE LAX-SFO MARKET



DATA: TABLE 3

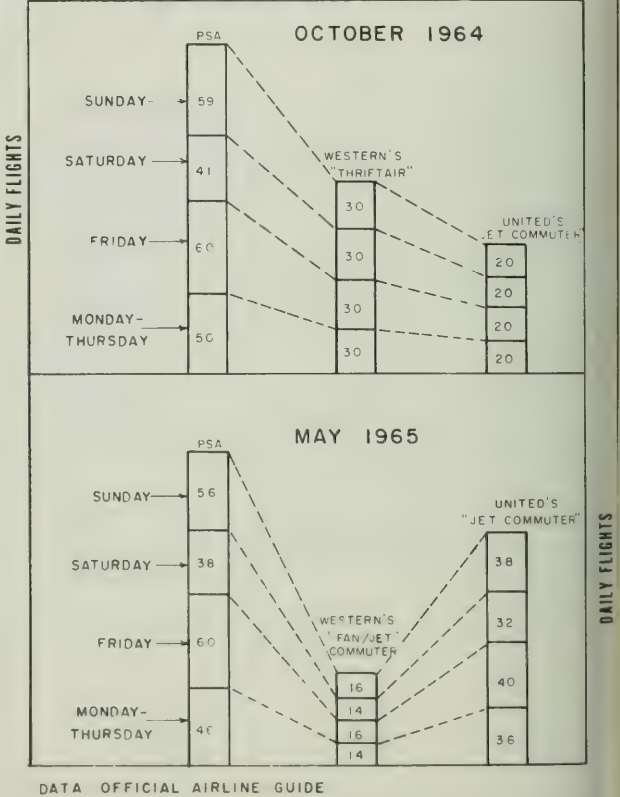
Fares and Competitive Shares

From the beginning, and till recently, Pacific Southwest Airlines maintained fares for its dense-configuration (90-seat Electras, for example) single-class service substantially below the coach fares of its trunk-airline competitors. In 1957 PSA's fare was \$10.99; trunk coach fares were \$14.85 (all fares include tax). In 1961, PSA's Electra fare was \$14.85; trunk airlines jet coach fares were \$20.30 till August, and then were raised to \$25.25. At present, PSA has the lowest fare on the route, \$12.00 for a one-hour flight in Electras. For a B-727 flight, PSA now charges \$14.18, the same as the trunk airlines' jet-commuter service (For detailed information on fares by class of service and kind of equipment see Table 9, Appendix A) The chart opposite shows the great differences in both level and trend, 1957 to 1964, between PSA's fares and average coach fares of its trunk airline competitors

With lower fares, PSA forged ahead in volume of traffic. But starting in 1962, the trunk airlines' determined competition in both quality of service and fares has brought them, together, equal with PSA in number of coach passengers. And these competitive efforts have, undoubtedly, expended total traffic far above what it might otherwise be.

PSA's success with dense configuration seating, 98 seats in Electras, 122 seats in their 727, supports the point of view that seat space is not an important factor affecting traffic - at least on short to medium stage-lengths

PSA STILL OFFERS MANY EXTRA FLIGHTS ON FRIDAYS AND SUNDAYS



Frequencies and Week-end Flights

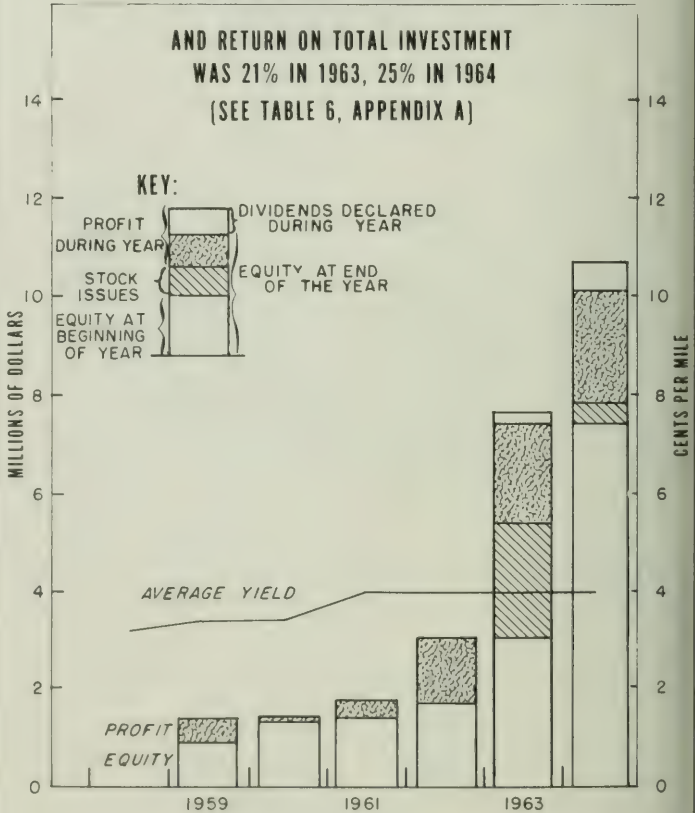
Pacific Southwest Airlines has always tried especially to attract heavy week-end traffic - to a far greater extent than the three competitive trunk airlines. PSA has many extra flights on Fridays and Sundays.

Friday and Sunday travel is probably for personal rather than for business reasons. ^APSA has thus appealed, successfully, to the large potential market - people who formerly traveled by other modes or did not travel at all.

A.

DESPITE LOW YIELD, PSA HAS A HIGH RETURN ON STOCKHOLDERS' EQUITY

AND RETURN ON TOTAL INVESTMENT
WAS 21% IN 1963, 25% IN 1964
(SEE TABLE 6, APPENDIX A)



Pacific Southwest Airlines Makes Money

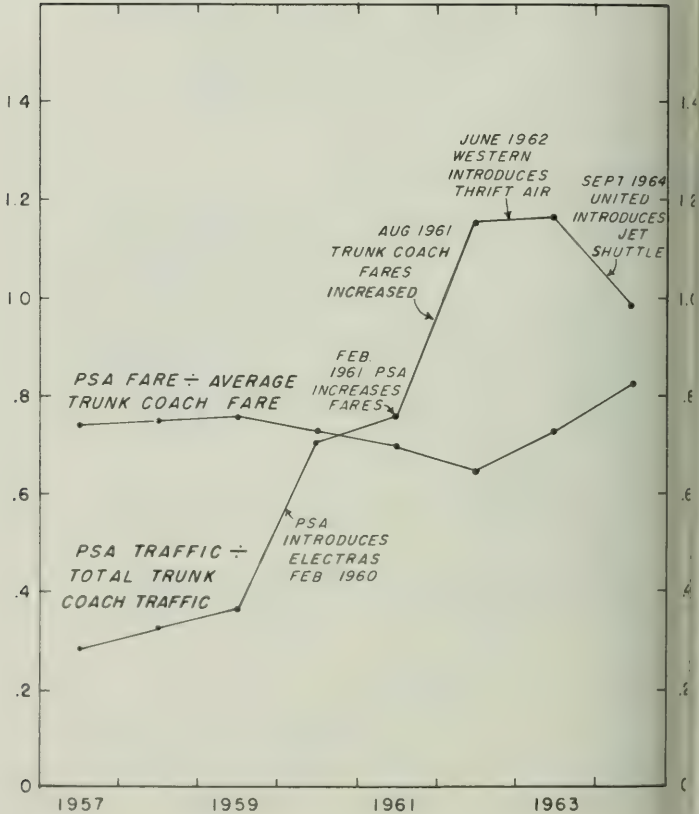
PSA's yield, per passenger-mile, is under 4 cents. Yet the firm has a good rate of return and has rapidly increased stockholder equity by plowing back substantial earnings

The bar chart opposite shows, for each year from 1959 through 1964, the equity at the beginning of the year (lower white portion) and the earnings during the year. Because nearly all earnings have been plowed back, the equity has grown by approximately the amount of the profit plus proceeds of new stock issues. Thus at the beginning of 1959, stockholder equity was slightly less than \$1 million; at the end of 1964 it was 10.1 million. Low earnings in 1960 and 1961 were due to speed restrictions and structural modifications of the company's Electras, and to losses incurred as a result of establishing service to Oakland airport (soon discontinued) with a DC-6B aircraft.

The company began to pay dividends in 1963 and increased them in 1964. Total dividends were \$204,290 in 1963, \$567,245 in 1964.

In 1964, PSA's return on stockholder equity was nearly 34%; return on total investment was 25%. (Further details are in Table 6, Appendix A.)

COMPETITION TAKES MANY FORMS



DATA: TABLE 4

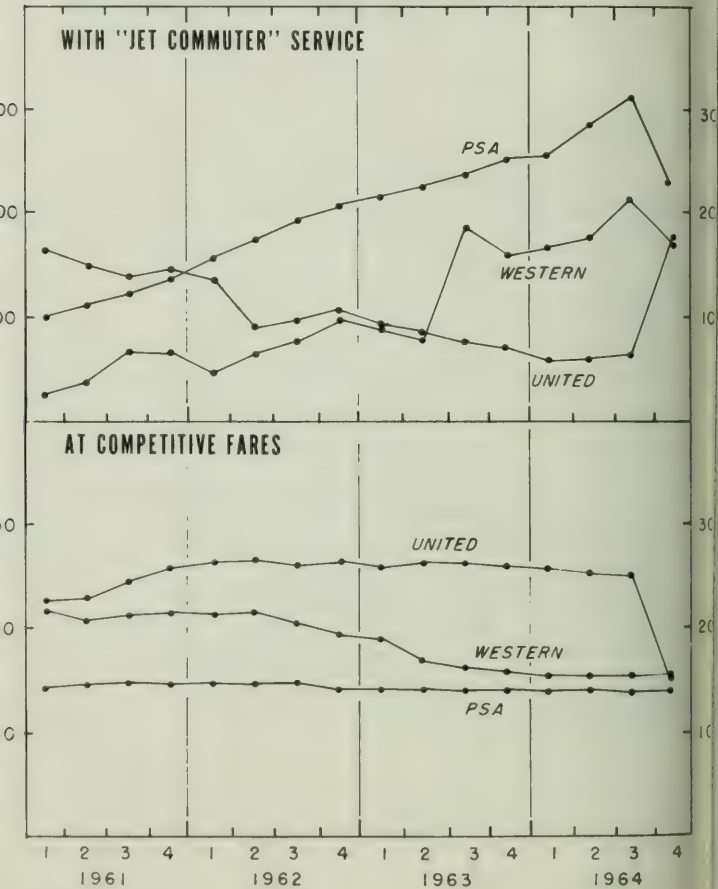
Multi-form Competition

Pacific Southwest Airlines has determinedly undercut fares of competitive air carriers. But keeping its equipment competitive, and the fare increases and decreases of the three trunk carriers, have also been highly important to PSA's progress in the market.

This chart shows, first, the ratio of PSA's traffic, year by year, to the three trunk airlines' coach traffic. The rising portion of the curve means that PSA was increasing its market share until 1964. The chart also shows the ratio of PSA's fare to the average coach fare of the trunk airlines. This ratio has always been below one, indicating PSA's consistently low fares. The ratio fell until 1962-63, when lower fares by PSA's competitors caused it to rise. Notice that PSA's traffic ratio rises as its fare ratio falls, and that the traffic ratio turns and falls as the fare ratio begins to rise in 1963-64.

But the chart also shows the timing and the apparent effect of other competitive moves, especially the introduction of superior equipment. Flying DC-3's and DC-4's at low fares, PSA made slow gains. The change over to Electras in early 1960, with a flying time of one hour at the same low fares, brought a dramatic increase of traffic. In the middle of 1961 the trunk air carriers raised jet coach fares from \$20.30 to \$25.25 (with tax), \$10.40 above PSA's \$14.85 fare for Electra service; PSA's traffic surged. Western Airlines' introduction of "Thrifair" service in slower DC-6B's at fares below PSA's, held up the progress of the intra-state airline. United Airlines' introduction, in late 1964, of "jet commuter" service in new B-727 jets at fares nearly as low as PSA's made a great change in competitive positions.

UNITED AIRLINES RECOVERS SHARPLY AT WESTERN'S AND PSA'S EXPENSE



DATA: TABLE 5

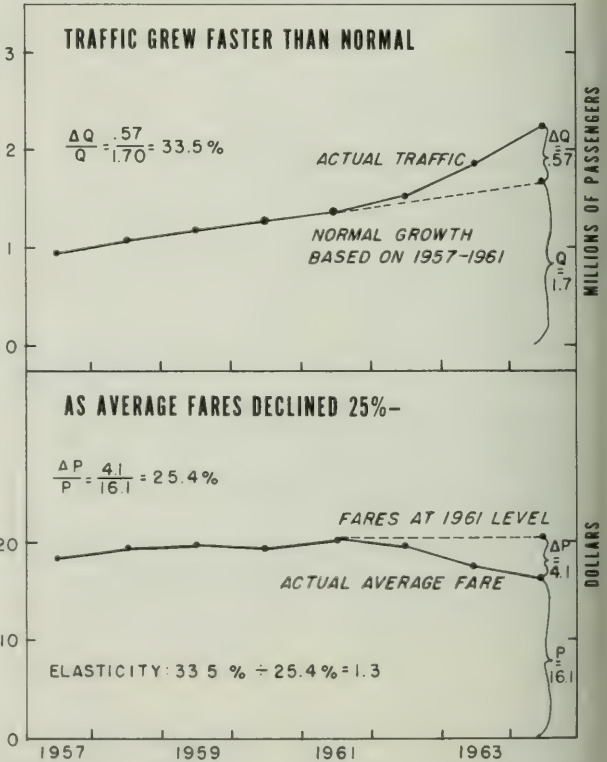
United Airlines' "Jet Commuter" Service

Long declining in the market, United Airlines made a powerful bid in September 1964 to regain its dominant competitive position. United offered "jet commuter" service in the new, three-jet B-727's at a fare of \$15.23, only a dollar above PSA's fare for Electra service. In April 1965 United reduced the fare to \$14.18, matching PSA's fare.

The effect was dramatic. United's traffic increased sharply at Western's and PSA's expense. This year, PSA has begun service with its own single B-727, flying 111 flights per week with the three-jet aircraft at load factors reportedly as high as 80 percent. Four more 727's are to be delivered to PSA this year, and another in early 1966. Meanwhile PSA has 291 additional weekly flights in Electras at fares of \$12.00 including tax - a total of 402 flights per week, a hundred more than any other carrier. Western dropped "Thriftair" and made a strong bid with jet service in B-720B's at competitive fares of \$14.18.

Accordingly, continued sharp competition in the market may be expected in 1965 to bring down fare levels still more, to expand traffic, and to improve equipment and service.

THOUGH TRAFFIC IS 70% BUSINESS, LAX-SFO MARKET IS PRICE-ELASTIC



DATA: TABLE 2, 7

The Fare-Elasticity of Demand

Studies by the airlines indicate that most of the travel on the Los Angeles-San Francisco route is for business purposes. The proportion is about 70 percent, somewhat above the national average. However, traffic appears to be elastic with respect to fares; declines of average fares bring more-than-proportional increases of traffic.

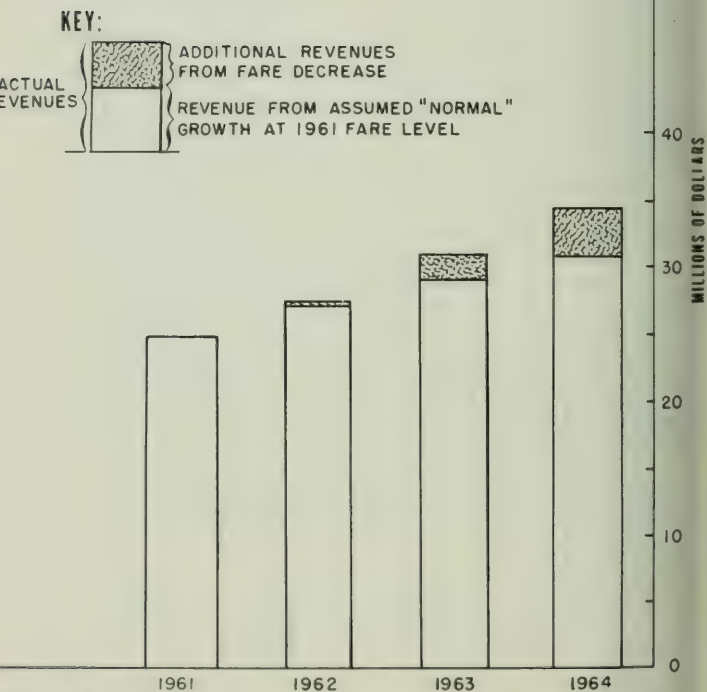
Pacific Southwest Airlines' always - low fares have attracted traffic from competitors, have induced fare reductions by them, have brought down average fares and have apparently expanded total traffic far above with it might otherwise be. This process implies that PSA has operated at relatively high load factors. Authentic information is not available, but high load factors would be consistent with PSA's brilliant earnings performance. Load factor of the Company's single 727 was reported above 80% in May 1965. Estimates based on revenue plane miles flown, seats per plane, and passenger-miles indicate system load factors for PSA of 71% in 1961, and 77% in 1962 and 1963. An estimate for the year 1964 based on flights, seats per flight, and passengers indicated a load factor of nearly 80%.

Estimating fare-elasticity of demand in a single market is especially difficult. However, if we take the smooth rise of traffic from 1957 to 1961 during which period fares did not change very much, as "normal" and as comprising all the other important factors influencing demand - growth of population and income, reduction of flying time, etc., we may impute the extra increase of traffic since 1961 to the fall of average fares and compute a fare-elasticity of 1.3. The detail of the computation is shown on the chart opposite and in Table 7, Appendix A.

This estimate may be low. The full effects on traffic of the decline of fares have not yet been felt. Many new air travelers have been initiated by the attractive low fares, and having flown once or twice they are far more likely to fly again. Accordingly, the fare-elasticity is probably a good deal greater for the longer run.

REVENUES IN THE LAX-SFO MARKET

LOWER FARES HAVE INCREASED TOTAL REVENUE
OF THE CARRIERS IN THE LAX-SFO MARKET

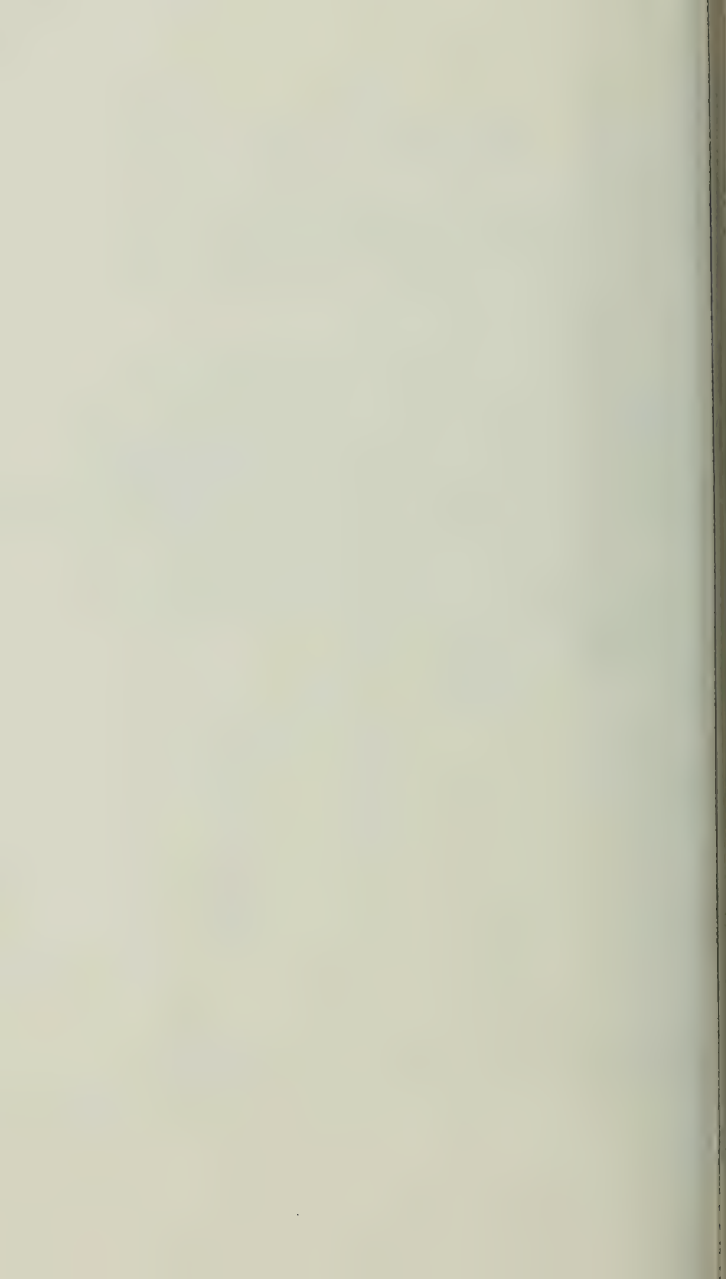


ATA: TABLE 8

Revenues in the Los Angeles - San Francisco Market

Revenues in the Los Angeles-San Francisco market increased from \$24 million in 1961 to \$34 million in 1964. The chart opposite however, shows that if the 1961 average fare level of \$18.41 (without-tax) had been maintained, normal growth would have produced \$30 million in revenues by 1964. Thus, the traffic stimulated by reductions resulted in additional revenues of \$208 thousand in 1962, \$2.1 million in 1963, and \$3.8 million in 1964. Since the market is price-elastic, further declines in fares would produce additional gross revenues for the carriers.

This is not to say however, that fare reductions would necessarily improve profits. Since unit costs would probably not decrease in proportion to the decline of yields, higher load factors would be necessary for the carriers to break even. But because of the intense competition in this market, higher load factors may be increasingly difficult to attain.



FEB 14 1967

BRIEF FOR RESPONDENT

IN THE
UNITED STATES COURT OF APPEALS
FOR THE NINTH CIRCUIT

No. 20,552

ISLAND AIRLINES, INCORPORATED, Petitioner,

v.

CIVIL AERONAUTICS BOARD, Respondent.

ON PETITION FOR REVIEW OF AN ORDER
OF THE CIVIL AERONAUTICS BOARD

DONALD F. TURNER,
Assistant Attorney General

O. D. OZMENT,
Deputy General Counsel,

ROBERT L. TOOMEY,
Acting Associate General Counsel
Litigation and Legislation,

TYLL VAN GEEL,
Attorney,
Civil Aeronautics Board,
Washington, D.C. 20428.

HOWARD E. SHAPIRO,
Attorney,
Department of Justice,
Washington, D.C. 20530

JOSEPH B. GOLDMAN,
General Counsel
Civil Aeronautics Board,
Washington, D.C. 20428.

FILED

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IN THE
UNITED STATES COURT OF APPEALS
FOR THE NINTH CIRCUIT

No. 20,552

ISLAND AIRLINES, INCORPORATED, Petitioner,

v.

CIVIL AERONAUTICS BOARD, Respondent.

BRIEF FOR THE RESPONDENT

JURISDICTIONAL STATEMENT

The jurisdiction of the Civil Aeronautics Board to issue the order here involved rested on Section 416(b) of the Federal Aviation Act of 1958 (72 Stat. 731, 49 U.S.C. 1301, et seq.). The jurisdiction of this Court is invoked under Section 1006 of the Federal Aviation Act, (49 U.S.C. 1486) which provides for the filing of a petition for review within 60 days after entry of the Board's order. The Board's order was entered on October 11, 1965, and the petition for review was filed on November 23, 1965.

COUNTERSTATEMENT OF THE CASE

Island Airlines, Inc. seeks review of an order of the Civil Aeronautics Board (R. 167) denying Island's request that it and all "others similarly situated" (R. 2) be exempt from economic regulation under the Federal Aviation Act with respect to air operations between the Hawaiian Islands. Island's proposal was that the Board surrender jurisdiction to the State of Hawaii to license and regulate those carriers engaged in

the transportation of persons and property between the islands. The application was filed on May 25, 1965, during the pendency before this Court of Island's appeal from the decision of the district court permanently enjoining it from operating without a certificate of convenience and necessity from the Board (235 F.Supp. 990), and was denied two weeks before this Court's affirmance of the district court decree. Island Airlines, Inc. v. Civil Aeronautics Board, 352 F.2d 735.^{1/}

As this Court is aware, the Federal Aviation Act establishes a pervasive system of regulation for air transportation, and vests exclusive regulatory jurisdiction in the Board over that transportation which falls within its coverage. Transportation between the Hawaiian Islands is subject to Federal control because the statute embraces (Section 401(10), 401(21), infra, p. 29) all carriage of mail by aircraft and "the carriage by aircraft of persons or property as a common carrier . . . between places in the same State of the United States through the airspace over any place outside thereof . . ." Furthermore the Act requires that any person desiring to engage in air transportation must first obtain a certificate of public convenience and necessity issued by the Board after notice and hearing and upon proof that the proposed transportation is required by the public convenience and necessity and that the applicant is qualified to perform it properly (Section 401(a), infra, p. 29). Carriers whose certificates authorize the transportation

^{1/} Island did not file a petition for certiorari to review this decision.

of mail may be granted subsidy for the support of their mail, passenger and property operations (Section 406(b), infra, p. 31). The statute also contains an exemption provision (Section 416, 49 U.S.C. 1376, infra, p. 32) which permits the Board to exempt any carrier or class of carriers from the economic regulatory provisions, including the requirement that a certificate of public convenience and necessity be obtained as a prerequisite to operations.^{2/} Pursuant to these various provisions, there are two carriers holding certificates from the Board which provide regular route operations between the islands and which receive subsidy support (Aloha Airlines, Inc. and Hawaiian Airlines, Inc.), and numerous carriers operating small aircraft between the islands pursuant to a blanket exemption regulation (14 C.F.R. 298) which permits certain "air taxi" operations.^{3/}

^{2/} To grant exemption, the Board must find that enforcement of the statutory provision (here, the one that a certificate be obtained) would result in "undue burden" or hardship on the carrier, and that exemption is in the "public interest."

^{3/} Generally speaking, certificates issues pursuant to Section 401 are required before regular route operations may be conducted with large transport aircraft. Hawaiian's original certificate was issued pursuant to the "grandfather" provisions of the Civil Aeronautics Act of 1938 (52 Stat. 987), and Aloha's certificate after proof of public convenience and necessity in 1948.

The "air taxi" regulation permits operations only with aircraft of less than 12,500 pounds gross takeoff weight, and any person desiring to do so may avail himself of the benefit of Part 298. Island proposes to operate with large transport-type aircraft, a type of service not permitted by Part 298.

The history of Island's attempt to establish that the Federal Aviation Act has no application to interisland operations except for the transportation of mail is familiar to the Court and need not be recounted here. For present purposes, it may be stated that Island's contentions in the prior litigation were not confined to the technical question of whether the channel waters between the islands are "high seas", with the consequence that operations between them involves passage "through the airspace over any place outside" the state. On the contrary, Island urged that even if the waters between the islands were outside the state's boundaries, the statute nonetheless should be held inapplicable because Congress could not have intended that the "any place" provision be applied to subject "local transportation" between the islands to Federal control,^{4/} and that such transportation was so much a matter of local concern and Hawaii's position so unique that the statute could not be constitutionally construed to vest jurisdiction in the Board. Additionally, it was contended that the state and Island had been discriminated against in various respects, and that there was no basis for any determination that operations by Island would inflict adverse competitive impact on the federally subsidized carriers Aloha and Hawaiian.^{2/} Notwithstanding Island's position, these various

^{4/} This was in fact the basis of the decision of the Hawaiian Supreme Court in holding that the state commission, rather than the Board, possessed jurisdiction. Application of Island Airlines, Inc., 17 Haw. 1, 382 P.2d 92 (1963).

^{2/} See, e.g., twelve errors asserted before this Court in the appeal from the District Court injunction (352 F.2d at p. 700).
(footnote continued)

contentions were rejected.

Thus, the District Court found that all of the major islands were separated by open seas which were outside the State's boundaries, and that the legislative history of the Statehood Act established that Congress intended operations over these waters to fall within the definition of interstate air transportation and to remain subject to economic regulation by the Board. It rejected Island's contention that,

They included:

"6. The Court below erred in failing to hold that either the Public Utilities Commission of the State of Hawaii or the State of Hawaii itself was an indispensable party to the action.

"7. The Court below erred in not dismissing the complaint upon the grounds that the Supreme Court of the United States is vested with original jurisdiction of actions to which a state is an indispensable party.

* * * * *

"9. The Court below erred in not holding that appellee's construction and application of the Federal Aviation Act resulted in unconstitutional and invidious discrimination against Hawaii, her people and appellant.

"10. The Court below erred in failing to hold that appellee was invidiously discriminating against Hawaii by attempting to enjoin appellant's flights on the basis of instrument clearances requiring it to fly to sea while not applying the same rule against California intrastate carriers, or alternatively, that appellee's conduct was (a) unjust and inequitable and constituted 'unclean hands,' or (b) showed such flights to be 'de minimis' and hence no basis for injunctive relief, or (c) constituted an administrative interpretation of the Federal Aviation Act showing such flights did not constitute a basis for federal jurisdiction.

"11. The Court below erred in finding that appellant's operations would result in a decrease in intervenors' revenues and an increase in their subsidy need without there being testimony in the record by witnesses on the stand and subject to cross-examination."

as thus construed, the Federal Aviation Act was unconstitutional. In view of the impact of Island's operations upon Hawaiian and Aloha, the court held that "to deny CAB jurisdiction would substantially interfere with the execution of aims and objectives of the Act", and thus "that Island's interisland flights are not a matter of purely local interest and concern." Accordingly, it issued a permanent injunction restraining Island from the carriage by aircraft of persons or property as a common carrier for compensation or hire in commerce, or engaging in air transportation, between the islands of Kauai, Oahu, Molokai, Lanai, Maui and Hawaii, of the State of Hawaii or between any combination of said islands,"without first being issued a certificate of public convenience and necessity by"the Civil Aeronautics Board (235 F.Supp. at p.1010). This Court affirmed.

While its appeal from the District Court injunction was pending, Island filed with the Board its application for an exemption from the certificate requirements of Section 401, as well as from all other economic regulatory requirements imposed by the Act. (R. 1) The application, filed pursuant to Section 416(b), alleged (1) that the need for adequate interisland service is especially great for local residents because of the geographical peculiarities of the State; (2) that existing interisland carriers primarily serve tourists traveling as part of a through journey from the mainland to the outer islands, and as a result the fare level is so high that their service places a damper on local traffic; (3) that this is primarily a local transportation problem and should be under the regulatory control of the local government; (4) that

the Board does not have jurisdiction over intrastate transportation generally and that its jurisdiction here is based on a technicality; and (5) that there is no significant federal function to be served by continued federal regulation.

Hawaiian (R. 38) and Aloha (R. 143) filed answers in opposition to Island's application, including statistical data with respect to interisland traffic, operating costs, fares, service, and estimates of the effect of third carrier competition. In general, it was their position that the market is too small to support three carriers; that an additional carrier or carriers in the market would substantially increase their subsidy requirements or fares or both; that existing service is adequate and is provided at reasonable fares; and that Island had failed to submit any facts to support the findings required by Section 416(b).

Island filed no reply to these answers nor did it request a hearing. Upon consideration of Island's application and the answers thereto, the Board found that Island had "not made a sufficient showing to warrant a grant of the exemption authority requested" (R. 168). It found nothing in Island's application to support Island's contention that a certificate proceeding would be an undue burden on that carrier or other carriers which might be authorized by the State of Hawaii to provide interisland air service, and no basis for concluding that enforcement of the economic regulatory requirements of the Act would not be in the public interest. Island, the Board said, had presented no facts indicating that existing service was inadequate; no details on

the size of the existing or potential market; and no facts as to why Island or any other carrier was better equipped than Hawaiian or Aloha to provide service designed for the resident market. Moreover, the Board continued, the operations of Hawaiian and Aloha required substantial federal subsidy assistance. Estimates submitted by these carriers indicated that Island's proposed service would result in diversion of up to \$4.8 million annually, thereby substantially increasing their subsidy need. Under these circumstances, the Board found that "it would not be in the public interest to grant exemption authority permitting a carrier or carriers to operate in direct competition with Hawaiian and Aloha." (R. 168). Finally, the Board rejected Island's contention that federal jurisdiction rested upon a mere technicality. It found that Congress had fully considered this question and had deliberately determined that federal regulation of interisland air transportation should continue. (R. 169).

Island did not petition for rehearing, and filed its petition for review herein on November 23, 1965.

STATUTES INVOLVED

The provisions of the Federal Aviation Act principally involved are set forth in the appendix to this brief, infra, p.29 et seq.

ARGUMENT

I. The petition for review presents no substantial issue which is open for consideration

In the final analysis, the basic thrust of Island's entire case is that interisland air carriage is not, or should not be, subject to

federal control and hence that the Court should direct the Board to issue an order relinquishing such jurisdiction in favor of the local authorities.^{6/} While couched in terms of an abuse of administrative discretion, Island's contentions--with the exception of an allegation of procedural error--are the same ones advanced by Island and rejected by the District Court and this Court in the injunction case. It argues that interisland air carriage is "intrastate in every substantial sense" (Br. p. 10) and hence a matter of local concern; that assertion of federal jurisdiction over such carriage results in "suffocation . . . of a state power which the state needs for its well being and which all other states possess" (Br. p. 16); that "'unusual circumstances' are abundantly present in the geography of Hawaii and its constitutional consequences", which cause a certification proceeding under Section 401 to be "an undue burden" within the meaning of Section 416 "because the Act does not cover the service described" (Br. p. 22); and that federal regulation of interisland air carriage unconstitutionally deprives the State of Hawaii of "equal footing" in the federal union (Br. pp. 29-33).

All of the foregoing arguments, and the variations on them which appear repeatedly throughout Island's brief, have been considered and rejected by this court within the past six months. It was determined

^{6/} Obviously the Court cannot direct the Board to exercise its discretion in a certain way. See Federal Power Comm'n v. Idaho Power Co., 344 U.S. 17 (1952); Federal Communications Comm'n v. Pottsville Broadcasting Co., 309 U.S. 134 (1940); State Airlines v. Civil Aeronautics Board, 174 F.2d 510 (C.A.D.C. 1949) reversed on other grounds, 338 U.S. 572 (1950).

in the injunction proceeding that interisland operations are not a matter of purely local concern because of their impact upon the two federally certificated carriers and hence upon the U.S. Treasury; that such operations do come within the coverage of the Federal Aviation Act; that this result was specifically intended by Congress; that Congress had the power to subject them to federal regulation; and that assertion of such power does not deprive the State of Hawaii of equal footing.

In sum, the parties in the instant proceeding are identical to those in the injunction litigation; the substantive issues are the same; and there has been neither change in the dispositive facts nor any intervening legal development. In these circumstances, we submit, the issues are res judicata (Sunshine Coal Co. v. Adkins, 310 U.S. 381, 401-404 (1940)) or else not open to consideration under the principle of collateral estoppel (Commissioner v. Sunnen, 333 U.S. 591, 597-603 (1948)). As a practical matter, however, it is unnecessary for the Court to determine whether the various technical requirements of res judicata or collateral estoppel are presented. It should be enough to know that no showing has been made which would warrant this Court's reconsidering issues which it considered less than six months ago and which it decided adversely to Island. Cf. Great Lakes Airlines v. Civil Aeronautics Board, 293 F.2d 153 (C.A.D.C. 1961).

7/ We do not mean, of course, that the decision in the injunction case would foreclose grant of an exemption with respect to a given interisland operation if the Board could make the findings required by the Act. Our point is simply that the basic allegations of error presently advanced with respect to the Board's denial of exemption in this case

Island's contention that the Board erred in failing to hold a hearing on its application is plainly barred from consideration by the Court, though for a different reason. As previously indicated, Island filed no reply controverting the allegations set forth in the answers of Hawaiian and Aloha to its application, it never requested a hearing, and did not seek reconsideration of the Board's order.^{8/} The carrier's failure to request a hearing and the complete absence of any showing of cause, let alone good cause, for such failure forecloses consideration of its contention that the Board should have ordered one sua sponte

Section 1006(e) of the Act (49 U.S.C. 1486(e), infra, p. 32) provides that "no objection to an order of the Board . . . shall be considered by the court unless such objection shall have been urged before the Board . . . or, if it was not so urged, unless there were reasonable grounds for failure to do so." Not only must objection be raised, but it must be raised in a timely manner. As the Supreme Court said in United States v. Tucker Truck Lines, 344 U.S. 33, 37 (1952):

"We have recognized in more than a few decisions, and Congress has recognized in more than a few statutes, that orderly procedure and good administration require that objections to the proceedings of an administrative agency be made while it has opportunity for correction in order to raise issues reviewable by the courts Simple fairness to those who are engaged in the tasks of administration,

^{8/} The Board's Rules of Practice provide that an applicant for exemption may file a reply to an answer opposing his application (14 C.F.R. 302.407). They also provide that the applicant may request a hearing on his application (14 C.F.R. 302.408). While the Rules of Practice do not specifically provide for petitions for reconsideration of orders denying exemption, they are frequently filed and entertained.

and to litigants, requires as a general rule that courts should not topple over administrative decisions unless the administrative body not only has erred but has erred against objection made at the time appropriate under its practice."

A similar situation was involved in Seaboard and Western Airlines v. Civil Aeronautics Board, 183 F.2d 975 (C.A.D.C., 1950), the only case in the Board's history, up until now, in which denial of an exemption has been the subject of a petition for judicial review. The Court's treatment of it is dispositive of Island's procedural objection:

"The present petition asks review of the Board's order denying a temporary exemption. The point to which petitioner's brief and argument are directed is that the Board failed to make adequate findings. Petitioner did not urge this objection before the Board, despite the fact that petitioner asked the Board for a rehearing on other grounds. The objection therefore comes too late. The statute provides that 'No objection to an order of the Board shall be considered by the court unless such objection shall have been urged before the Board or, if it was not so urged, unless there were reasonable grounds for failure to do so.' 52 Stat. 1524, 49 U.S.C. §646(e). No such grounds are shown. It follows that we could not modify or set aside the Board's order even if we regarded the objection now urged as valid."

II. The Board's denial of exemption from the Act was a reasonable exercise of administrative discretion

A. The exemption power generally and in relation to the Hawaiian statehood legislation

Island argues that the Federal Aviation Act contemplates a "program of exemption" in addition to certification and other economic regulation (see, p. 7), and that the Board erred in failing to establish such a "program" under which regulation of interisland air carriage would be left to local authority. The contention is at war with the Federal Aviation Act and the Hawaiian statehood legislation.

As Judge Frankfurter has observed, the certification and exemption provisions are not "merely two alternative methods by which the Board

can authorize operation". American Airlines v. Civil Aeronautics Board, 231 F.2d 483, 488 (C.A.D.C. 1956). On the contrary, "[t]he basic concept of the statute . . . is . . . a certificated system. American Airlines v. Civil Aeronautics Board, 235 F.2d 845, 850 (C.A.D.C. 1956) cert. denied, 353 U.S. 905.^{9/} In other words, certification is the "normal" method for authorizing those significant services which Congress has chosen to subject to the Act. Pan American World Airways v. Civil Aeronautics Board, 261 F.2d 754, (C.A.D.C. 1958), cert. denied, 359 U.S. 912. Thus, Island completely misconceives the nature and scope of Section 416(b) and its place in the statutory scheme established by the Federal Aviation Act. Its contention is, in effect, precisely the one rejected by the court in American Airlines, supra, 235 F.2d at p. 850.

" . . . Congress did not intend that the Board might, by the use of the exemption provisions of Section 416(b), destroy the elaborate basic requirements of the Act for a certificated

^{9/} This case eventually led to legislation (P.L. 87-528, 87th Cong. 2d Sess., 76 Stat. 143) during the consideration of which Congress expressed views as to the exemption power which are wholly at odds with Island's concept of the power. As the court's opinion reveals, the Board had granted exemptions to a number of carriers to engage in "supplemental air transportation". The court reversed, holding the exemptions invalid. Thereafter, the Board issued certificates of public convenience and necessity authorizing the same service and this action was held by the court to be in excess of the Board's statutory authority. (United Airlines v. Civil Aeronautics Board, 279 F.2d 446 (C.A.D.C. 1960)). As a result, legislation was introduced to amend the Act so as to empower the Board to issue certificates for such service. The history of that legislation reflects complete agreement with the court in reversing the exemption order. Thus, the Conference Committee reported that "the hearing records of both Houses are replete with evidence that the Board has exceeded the proper use of the exemption authority . . ." It added that the exemption power under Section 416 "should be construed narrowly and employed in only very limited and unusual circumstances." (H.R. Rep. No. 1950, 87th Cong., 2d Sess., p.13).

system of airplane carriage Despite the broad language of Section 416(b), we think it perfectly clear that Congress did not set up so elaborate a series of provisions in respect to the certification of carriers, and the public interest, convenience and necessity therein involved, and at the same time grant its administrative agency power to destroy those elaborate provisions."

In short, "the Board . . . may not unduly impinge upon the certificated system by use of the exemption power" (235 F.2d at p. 850).

To be sure, the Board has promulgated various so-called blanket exemption regulations permitting various types of carriers to operate without obtaining certificates of convenience and necessity and, in varying degrees, without compliance with other regulatory provisions. Examples include the present air taxi regulation (14 C.F.R. 298) under which operators of small aircraft may engage in air transportation throughout the United States, including Hawaii.^{10/} The Board also at one time permitted various irregular and specialized services with large aircraft pursuant to a blanket exemption. See 14 C.F.R. 291 (1949 Ed.), 14 F.R. 3546, 6807; 14 C.F.R. 295 (1949 Ed.), 14 F.R. 3552.

However, in all of these situations the operations were deemed to be such as not to "unduly impinge upon the certificated system." Here, there would not only be an exemption under which the Board would surrender its authority to the state, but one which contemplates the use of large transport aircraft in direct competition with the certificated and sub-subsidiary operations of Alana and Hawaiian. Plainly, the Board was not required to accede to this request.

^{10/} See 14 C.F.R. 298.2, 298.21(b) and (e).

The notion that there should (indeed, according to Island, must) be a "program of exemption" with respect to interisland operations also flies in the face of the legislative history of the statehood legislation. The Board was plainly right in stating in its order denying exemption (R. 168) that "the Congress of the United States in enacting the Hawaii Statehood Bill . . . fully considered the regulatory problem and determined that because of the geographic situation, federal regulation of the interisland air transportation should continue." As the District Court observed in the injunction proceeding, the legislative history of the Statehood Bill reflects a clear Congressional intent "that inter-island flights . . . were expected to fall within the scope and control of the Act", and that these operations "are not of purely local interest and concern" (235 F.Supp. at p. 1010).^{11/} This Court agreed, pointing out that "the Congress, by the statute, assumed jurisdiction over this area.^{12/} This it had the power to do. In this field, it has supremacy." In

^{11/} In reporting on the Statehood Bill, the Senate Committee stated as follows: "In the other States, air transportation of this kind passing through airspace outside the State is of slight volume in comparison with air transportation merely between places in the same State. In the case of Hawaii, the reverse would be true. The committee wishes to make it clear that it believes the application of the provisions of the Federal Aviation Act and other applicable Federal legislation to the State of Hawaii should continue in accordance with the definition of interstate air transportation as contained in that act." S. Rep. No. 80, 86th Cong., 1st Sess. (emphasis added). See, also, Hearings, Senate Committee on Interior and Insular Affairs, on S. 50, 86th Cong., 1st Sess., relevant excerpts from which are quoted at pages 18-20 of the Board's brief in this Court in Island Airlines v. Civil Aeronautics Board, No. 19,752.

^{12/} Quoting United Airlines v. Public Utilities Comm'n, 109 F.Supp. 13 (N.D. Cal. 1952), reversed on other grounds, 346 U.S. 402 (1953).

short, it is settled that Congress specifically focused on the question and deliberately determined that interisland air transportation should remain subject to federal jurisdiction and control.

In the light of the foregoing, it is obvious that acceptance of Island's theory would completely nullify the Congressional intent in specifically subjecting interisland operations to the certification and other regulatory requirements of the Act. Congress was fully aware of the considerations advanced by Island in support of the view that the federal interest in such operations is slight, and therefore that federal jurisdiction should be forsworn. It nevertheless determined to preserve federal regulation. It simply makes no sense to argue that, while deliberately preserving federal regulation over interisland operations, Congress at the same time contemplated establishment of a "program of exemption" under Section 416(b) under which the Board would totally dispense with federal regulation.

B. Island's application and the Board's findings with respect to it

The showing which an applicant for exemption must make is set forth in Section 416(b) itself. There must be a showing upon which the Board can predicate a finding that enforcement of the provisions of the Act from which exemption is sought would be "an undue burden" on the applicant because its "operations" are either of "limited extent" or affected by "unusual circumstances". In addition, the Board must be able to find that enforcement of the Act "is not in the public interest". The Court of Appeals of the District of Columbia Circuit

has held that, "in the absence of any one of these findings, the Board is not authorized to suspend the normal statutory requirements of notice, hearing and requisite findings for issuance of a certificate of public convenience and necessity."^{13/}

It would be impossible (and, for purposes of this appeal, pointless) to catalog here all of the types of situations in which the Board has determined that an exemption from the certificate requirements of the Act (i.e., permitting new service) is justified. Among the factors considered by the Board in determining that an exemption is warranted have been (1) the existence of an immediate and unfilled public need for service of such urgency that a certificate proceeding would unduly delay fulfillment of the need;^{14/} (2) the temporary or sporadic character of the service;^{15/} (3) the experimental character of the service;^{16/} or (4) because of rapidly changing demands, the need for flexibility in performance of the service, a need which would be hampered by repeated certificate amendment proceedings.^{17/} Moreover,

^{12/} For American World Airways v. Civil Aeronautics Board (supra, 261 F.2d at 757).

^{14/} E.g. Mackey Airlines, Exemption, 26 C.A.B. 709 (1957); Mohawk Air. Ogdenburg, Exemption, 25 C.A.B. 766 (1957).

^{15/} United Air Lines, Exemption, 25 C.A.B. 782 (1957); Lake Central, North Central, St. Joseph/Benton Harbor, Exemption, 30 C.A.B. 1542, (1959); Application of Starflite, Inc., Order E-21535 (1964).

^{16/} Surface-Mail-By-Air, Exemption, 20 C.A.B. 658 (1955); affirmed, American Airlines, et al. v. Civil Aeronautics Board, supra, 231 F.2d 483.

^{17/} Los Angeles Airways, Certificate Renewal, 14 C.A.B. 284, 288 (1951); Service to Santa Catalina Island, 30 C.A.B. 1060, 1077 (1960).

as the cases cited disclose, the Board customarily takes into consideration the competitive impact which the proposed service would have upon existing carriers operating pursuant to certificates of public convenience and necessity. Island's application presented no facts or supporting data, ^{18/} remotely suggesting the existence of such factors. Rather, it sought complete relinquishment of federal control so that it, and all other carriers similarly situated, might engage in a regular, scheduled service, so far as the Federal Government would be concerned, on a permanent basis. With the exception of extended argument with respect to the alleged lack of federal interest in interisland transportation, and "policy" favoring local regulation of local commerce (R.20), its application rested upon the bald assertion, wholly unsupported by any factual detail, that there exists a need for interisland service in addition to that being provided by Hawaiian and Aloha. As the Board said:

"Island has not presented any facts which would indicate that existing service is inadequate to meet the air service needs of Hawaiian residents. The application does not contain any details on the size of the existing or potential market, nor does Island submit any facts on why it or any other carrier might be better equipped than Hawaiian and Aloha to provide service designed for the resident market" (R. 168).

^{18/} The Board's procedural regulations require that exemption applications "shall state in detail the facts relied upon to establish that the enforcement of the provisions from which an exemption is sought would be an undue burden upon the applicant by reason of the limited extent of, or unusual circumstances affecting the operations of such applicant and that enforcement of such provision is not in the public interest." (14 C.F.R. 302.402(b)). They also require that the application "be accompanied by a statement of economic data or other matters which the applicant desires the Board to officially notice, and by affidavits establishing such other facts as the applicant desires the Board to rely upon." (14 C.F.R. 302.402(c)).

In other words, apart from its "federal-state policy" arguments, Island alleged only, and in conclusory form at that, that more interisland service was required by the public convenience and necessity. This is, of course, precisely the purpose of the certificate provisions of the Act. Thus, Island's showing left the Board little, if any, alternative but to find that the carrier had made "no showing that exemption of Island and all other carriers authorized by the Hawaiian State Government to provide interisland air service would be in the public interest, nor that a certificate proceeding would be an undue burden on Island or such other carriers" (R. 168).^{19/}

Not only had Island failed to make any factual showing upon which the Board could predicate the findings required by Section 416(b) as a prerequisite to exemption, but the Board found affirmatively that an exemption would be contrary to the public interest (R. 168):

"In addition, the Federal Government has a substantial interest in the problems of interisland air transportation, which could be adversely affected by the exemption requested. Since 1949 it has paid \$6,377,000 in subsidy to the two interisland carriers. Aloha estimates that Island's proposed service

^{19/} Even in its brief here, Island completely ignores the lack of any showing in these respects. It argues only that "'unusual circumstances' are abundantly present in the geography of Hawaii and its constitutional consequences" and that these circumstances cause an "undue burden" within the meaning of Section 416(b) (Br. p. 22). The undue burden is asserted to be that "a certification proceeding . . . [would be] foredoomed because the Act does not cover the service described If the service is not within the Board's authority to certify, it is not within the Board's authority to exclude, and any obligatory proceeding to invoke Board action beyond its powers would be an undue burden" (*ibid.*). In view of the decision of the District Court and this Court in the injunction proceeding, these assertions are without merit. The specific holding there was, of course, that, notwithstanding the "unusual circumstances" now relied upon by Island, the Act does cover the service described, and hence is within the Board's regulatory authority.

would divert \$1,000,000 annual revenue from Aloha, and Hawaiian estimates that the two subsidized carriers would lose an additional \$4,856,000 annually as a result of Island's service. These diversion estimates are based on Island's service alone, while the application presents the possibility of an even greater number of additional carriers in the market. Under these circumstances, it would not be in the public interest to grant exemption authority permitting a carrier or carriers to operate in direct competition with Aloha and Hawaiian."

Contrary to Island's contentions, the relevance of these considerations is obvious. Section 102 of the Act (49 U.S.C. 1302, infra, p. 29) directs the Board to consider a number of factors "as being in the public interest". Among these are the development of an economically sound air transportation system, properly adapted to the needs of the foreign and domestic commerce of the United States, of the Postal Service, and of the national defense. Hawaiian and Aloha, both operating pursuant to certificates issued by the Board, are a part of the national air transportation system. Thus, diversionary impact of competitive services upon them is manifestly relevant to the preservation of sound economic conditions in the system. Moreover, where, as in the case of Hawaiian and Aloha, the service is subsidized, the effect of revenue diversion upon the Federal Treasury necessarily looms large in determining wherein lies the public interest. Thus, from the earliest days, the Board has taken these factors into consideration in determining whether competitive service should be authorized, both in certificate proceedings and in passing upon exemption applications. ^{20/} Further, in American Airlines v. Civil

^{20/} In addition to the various exemption cases cited, supra, p. 17, see, e.g., Ala. Trans. Air., Twin Cities-St. Louis Operation, 2 C.A.B. 63, 88 (1947); Florida East. Ry. v. C.A.B. 745, 774 (1946); Hawaiian Intraterrestrial Service, 10 C.A.B. 62, 65-66 (1948).

Aeronautics Board, supra, 235 F.2d at p. 851, the Court emphasized the importance of the impact upon certificated carriers as a factor to be considered by the Board in granting exemptions.^{21/} Moreover, in the injunction proceeding it was specifically held that the potential diversion of traffic from Aloha and Hawaiian and the resultant increase in the claims of those carriers for subsidy support were precisely the reasons that Island's interisland flights are a matter of federal concern (235 F.Supp. at p. 1010). In these circumstances, we submit, the Board's findings with respect to the potential impact upon Aloha and Hawaiian were obviously relevant to, and supported, the Board's determination that relinquishment of federal jurisdiction over competing carriers would not be in the public interest.^{22/}

^{21/} In agreeing with the Board's determination in that case that the service in question was in the public interest, the Court did so upon acceptance of the Board's finding that the "proposed supplemental service will not result in adverse economic effects upon the certificated system", and "the assurance of the Board that it will not hereafter permit adverse economic effects to jeopardize the certificated system or to pose a substantial threat to it." (235 F.2d at p. 851). The Court stated that "this is required by the general scheme of the statute" (235 F.2d at p. 850).

^{22/} Island asserts in this connection that neither Aloha nor Hawaiian "has proved, under the conditions of Hawaiian Statehood, a case of public convenience and necessity", and that the Board has "covered [them] with an impenetrable blanket of competitive immunity on grounds of an earlier public interest which the CAB has never reviewed since the change in Hawaii's status and which now is exclusively Hawaii's function to determine" (Br. p. 21). By "conditions of Hawaiian Statehood", we assume Island means the alleged lack of federal interest in interisland air carriage, a contention laid to rest in the injunction proceeding. Similarly laid to rest was the contention that it is now "exclusively Hawaii's function to determine" the public interest factors involved in interisland air carriage.

(footnote continued)

Island suggests that the Board's finding of potential impact of additional interisland service upon Hawaiian and Aloha is undercut by a study prepared by the Board's staff relating to air travel between Los Angeles and San Francisco (Appendix B to Island's Brief).^{23/} This study, which does "not necessarily reflect official views or opinions of the Board Members themselves", is designed "to throw light on the factors generating air passenger traffic" (Br. p. 9a). It in no way detracts from the Board's judgment.

It is true that Hawaiian's basic authority is a "grandfather" certificate. This authority, however, has been amended under the public convenience and necessity standard and, moreover, Aloha's certificate was issued only after proof of public convenience and necessity. Statehood has no effect on the proof or findings required under that standard. The Board normally considers the needs of intrastate travel in certificate proceedings. See, e.g., Frontier Airlines v. Nebraska Department of Aeronautics, 175 Neb. 524, 122 N.W. 2d 476 (1963); Southwestern Area Local Service Case, 30 C.A.B. 1318, 1326-1332 (1959).

To the extent that Island may be suggesting that the Board should decertify Aloha and/or Hawaiian, we merely note that Section 401(g) (49 U.S.C. 1371(g)) authorizes revocation of a certificate only for intentional violations of the Act.

^{24/} We note Island's reference (Br. p. 36, n. 26) to the fact that one of the carriers providing service between Los Angeles and San Francisco is Pacific Southwest Airlines, the intrastate carrier involved in C.A.B. Friedman Aeronautics, 246 F.2d 173 (1957), in which this Court held that operation physically confined within the boundaries of a single state nevertheless be interstate air transportation for which authority from the Board is required. While it is of no particular moment, Island is mistaken in asserting that the Board has not, since that case, had occasion to proceed against PSA for violations of the Federal Aviation Act. On June 10, 1963, the Board issued a cease and desist order (E-196) restraining the carrier from carrying on its intra-California flights a substantial number of persons whose journeys commenced or terminated at points outside of California.

It is self-evident (and the staff study bears this out) that a new service will normally divert revenues from existing carriers.^{24/} To be sure, competition sometimes results in traffic growth. As the study itself points out, however, "historical [traffic] change is [a] compound of many factors" (Br. p. 9a). It by no means follows, moreover, that an increase in the amount of traffic will offset the diversion from existing carriers. Whether there will be traffic growth and whether it will offset the diversionary impact upon existing carriers depends upon such factors as the existing size and potential of the market, the pattern of service offered, and the like. Island presented no facts upon which an estimate could be made in this regard.^{25/} Moreover, as the Board emphasized, Island's proposal was for wholesale competition by an unlimited number of carriers. In these circumstances, we submit, there is no basis for Island's complaint that the Board's judgment with respect to the impact upon Hawaiian and Aloha of relinquishment of all federal control over competition with these carriers.

As previously indicated, with the exception of the alleged need for additional interisland service, Island's entire case for exemption rested upon constitutional policy arguments that such transportation should not

^{24/} Indeed, in the injunction proceeding, the District Court "accept[ed] the government's statement that there would be a very substantial decrease in revenues to the two carriers (estimated at well over \$3,000,000 annually)", and that "any substantial loss of revenue would materially increase the claims of the two carriers for subsidy support" (235 F.Supp. at p. 1009).

^{25/} It did not even rely on staff study in its presentation to the Board. Moreover, a study of "the heaviest traveled of all city-pair markets in the world" would have little materiality on the ability of interisland markets to support multiple competition.

be subjected to federal regulation, and it contends that "the Board . . . committed flagrant error in refusing even passing notice of the state's contention that the public interest called for preservation of local power over local commerce" (Br. p. 16). The Board specifically dealt with this question, finding that it had been disposed of by Congress itself (R 168-169). We have already shown that the Board was clearly right. It will suffice to repeat at this point what has already been demonstrated, namely, that Congress was fully aware of the consideration advanced by Island, and nevertheless deliberately chose to subject interisland transportation to federal regulation, a decision which this Court specifically held to be within Congress' constitutional power. ^{26/}

Contrary to Island's contention (Br. pp. 25-27), the Board's decision in this case is not inconsistent with Catalina Island Service Investigation, Order E-19678 (1963) or Application of Starflite, Inc., Order E-21535 (1964). As Island frankly conceded before the Board, the Catalina Island case was not based upon the "intrastate quality of the

^{26/} Island's argument (Br. pp. 29-33) that application of the Act is an unconstitutional violation of the "equal footing" doctrine (Coyle v. Smith, 221 U.S. 559 (1911)) was specifically raised and rejected in the injunction proceeding. The Court there stated (352 F.2d at p. 744) that "we find no 'invidious discrimination' against the State of Hawaii. Equal boundaries to each state are not necessary". United States v. Louisiana, 368 U.S. 1, 77 (1960)". In the case cited by the Court, the Supreme Court specifically rejected an "equal footing" contention.

While the "equal footing" contention is foreclosed by the decision in the injunction case, a word is in order with respect to Interior Airways v. West Alaska Airlines, 188 F.Supp. 197 (D.C. Alaska 1960) cited by Island (Br. pp. 30-31). The critical distinction between that case and this one is that the transportation there involved was not "interstate" within the meaning of the Act, whereas interisland transportation is.

service authorized . . . and the two situations are not wholly parallel" (R. 24). Similarly, in Starflite the Board's decision was not predicated upon the view that the operations were of local concern and hence should be left to local regulation. Moreover, the operations exempted involved only occasional passage through the airspace of a place outside of the state because of weather conditions, and there was no problem of competitive impact upon other carriers.^{27/}

III. There was no irregularity
in the Board's procedure

As previously indicated, despite the existence of regulations permitting it to do so, Island filed no reply to Hawaiian's and Aloha's answers to its application, nor did it request a hearing. Apart from the fact that the carrier's failure to request a hearing forecloses consideration of its contention here that a hearing should have been held, such failure is a fair measure of the merits of the contention.

Numerous provisions of the Act--including Section 401(c) which governs proceedings on applications for certificates of public convenience and necessity and which is the basic provision from which Island sought exemption--require a hearing prior to Board action. In

^{27/} Island's reliance on Motor Carrier Operation in the State of Hawaii, 84 M.C.C. 5 (1960) is misplaced. There, a closely divided Commission, acting pursuant to a statutory provision specifically empowering the Commission to determine whether interstate and foreign commerce was of sufficiently insubstantial federal interest to warrant exemption from federal regulation in favor of local regulation, found "no useful purpose" in federal regulation. Here Congress affirmatively determined for itself that interisland air carriage should remain subject to federal regulation, and it has been judicially determined that there is a substantial federal interest in such regulation.

marked contrast, Section 416(b) does not and it has been uniformly held that none is required. Eastern Air Lines v. Civil Aeronautics Board, 185 F.2d 426 (C.A.D.C. 1950), vacated as moot, 341 U.S. 901; Cook Cleland Catalina Airways v. Civil Aeronautics Board, 195 F.2d 206 (C.A.D.C. 1952) ^{28/} American Airlines v. Civil Aeronautics Board, supra, 231 F.2d 483. As the court observed in Eastern, "[t]here would be small point in permitting the Board to exempt a carrier from the delay and other burdens of a full hearing under §401(h) and at the same time requiring the Board, before granting the exemption, to hold a similar full hearing under §416(b)(1)" (185 F.2d at 428).

In an effort to avoid the dispositive effect of these decisions, Island suggests that the Eastern case turned upon the fact that "there were proceedings, in the course of which several verified documents were filed with the Board" (185 F.2d at 428), and that "no such proceedings were had before the Board in Island" (Br. p. 36). The "proceedings" involved in Eastern were precisely the same as those involved here with the possible exception that the documents filed in this case--including Island's--were not verified. Obviously, the Court's decision in Eastern did not turn upon this factor, and it may be added that the Court there held "that these proceedings were all the law requires and more" (185 F.2d at p. 428). ^{29/}

^{28/} Gr. Springfield Airport Authority v. Civil Aeronautics Board, 244 F.2d 377 (C.A.D.C., 1956); Nebraska Dept. of Aeronautics v. Civil Aeronautics Board, 242 F.2d 226 (C.A. 8, 1956).

^{29/} As Island itself recognizes, any contention that the rule articulated in Eastern is applicable only to competitors objecting to the grant of an exemption is foreclosed by Cook Cleland.

Island also suggests that Cook Cleland turned upon the fact that the Board treated as true all of the applicant's allegations of fact, and that, in contrast, the Board rejected Island's factual allegations, "accepted facts alleged but not proved by the opposition, and made such unproved facts the basis of decision" (Br. p. 37).^{30/} The carrier is wrong on all counts. The Court held in Cook Cleland that "exactly the same reasoning" adopted in Eastern applied there, and in Eastern there were sharply contested factual issues. Moreover, the facts alleged by Hawaiian and Aloha in opposition to grant of Island's application were never contested by Island, notwithstanding that it had ample opportunity to do so. Thus, to the extent that those facts entered into the Board's decision,^{31/} Island has no basis for complaint.

Finally, we note Island's suggestion (Br. p. 37) "that a sound statement of current law on the right to a hearing at the administrative level in the absence of statutory provision therefor is found in the

^{30/} Apparently Island would perceive no error if the Board had accepted the "facts alleged but not proved" in its own application.

^{31/} Even now, Island does not indicate what purpose a hearing would serve, save to call to the Board's attention the staff study relating to the Los Angeles, San Francisco market (see, supra, p. 22). As previously indicated, this study would have little, if any, materiality to the impact upon Hawaiian and Aloha of competition by Island and other carriers. Moreover, Island was free to call this to the Board's attention prior to the Board's decision and failed to do so. To be sure, the study was published subsequent to the time called for by the Board's Rules of Practice for a reply to the answers of Hawaiian and Aloha. However, the Rules specifically provide that leave to file otherwise unauthorized documents may be obtained for good cause shown (14 C.F.R. 302.4(f)) and discovery of "new evidence" not theretofore available is often treated as good cause.

Court's opinion in First Nat. Bank of Smithfield, N.C. v. First Nat. Bank of E.N.C., 232 F Supp. 725 (E.D.N.C., 1964)." The short answer is that that case has been reversed on the precise point for which Island cites it (First Nat'l Bank of Smithfield, North Carolina v. Saxon, 352 F.2d 26 (C.A. 4, 1965)), and the "current law" on the subject remains Eastern, Cook Cleland, and American.

CONCLUSION

The Board's order should be affirmed.

Respectfully submitted,

DONALD F. TURNER,
Assistant Attorney General,

O. D. OZMENT,
Deputy General Counsel,

ROBERT L. TOOMEY,
Acting Associate General Counsel
Litigation and Legislation,

HOWARD E. SHAPIRO,
Attorney,
Department of Justice,
Washington, D.C. 20530

TYLL VAN GEEL,
Attorney,
Civil Aeronautics Board,
Washington, D.C. 20428.

JOSEPH B. GOLDMAN,
General Counsel,
Civil Aeronautics Board,
Washington, D.C. 20428.

Dated: March, 1966

APPENDIX

Relevant provisions of the Federal Aviation Act of 1958,

72 Stat. 731, as amended, 49 U.S.C. 1301 et seq., are:

TITLE I - GENERAL PROVISIONS

DEFINITIONS

Sec. 101 [72 Stat. 737, as amended by 75 Stat. 467, 76 Stat. 143, 49 U.S.C. 1301] As used in this Act, unless the context otherwise requires--

* * * * *

(10) "Air transportation" means interstate, overseas, or foreign air transportation or the transportation of mail by aircraft.

* * * * *

(21) "Interstate air transportation", "overseas air transportation", and "foreign air transportation", respectively, mean the carriage by aircraft of persons or property as a common carrier for compensation or hire or the carriage of mail by aircraft, in commerce between, respectively--

(a) a place in any State of the United States, or the District of Columbia, and a place in any other State of the United States, or the District of Columbia; or between places in the same State of the United States through the airspace over any place outside thereof; or between places in the same Territory or possession of the United States, or the District of Columbia;

(b) a place in any State of the United States, or the District of Columbia, and any place in a Territory or possession of the United States; or between a place in a Territory or possession of the United States, and a place in any other Territory or possession of the United States; and

(c) a place in the United States and any place outside thereof;

whether such commerce moves wholly by aircraft or partly by aircraft and partly by other forms of transportation.

* * * * *

DECLARATION OF POLICY: THE BOARD

Sec. 102. [72 Stat. 740, 49 U.S.C. 1302] In the exercise and performance of its powers and duties under this Act, the Board shall

consider the following, among other things, as being in the public interest, and in accordance with the public convenience and necessity:

(a) The encouragement and development of an air-transportation system properly adapted to the present and future needs of the foreign and domestic commerce of the United States, of the Postal Service, and of the national defense;

(b) The regulation of air transportation in such manner as to recognize and preserve the inherent advantages of, assure the highest degree of safety in, and foster sound economic conditions in, such transportation, and to improve the relations between, and coordinate transportation by, air carriers;

(c) The promotion of adequate, economical, and efficient service by air carriers at reasonable charges, without unjust discriminations, undue preferences or advantages, or unfair or destructive competitive practices;

(d) Competition to the extent necessary to assure the sound development of an air-transportation system properly adapted to the needs of the foreign and domestic commerce of the United States, of the Postal Service, and of the national defense;

(e) The promotion of safety in air commerce; and

(f) The promotion, encouragement, and development of civil aeronautics.

* * * * *

TITLE IV--AIR CARRIER ECONOMIC REGULATION

CERTIFICATE OF PUBLIC CONVENIENCE AND NECESSITY

Certificate Required

Sec. 411. [72 Stat. 754, 49 U.S.C. 1371] (a) No air carrier shall engage in any air transportation unless there is in force a certificate issued by the Board authorizing such air carrier to engage in such transportation.

Application for Certificate

(b) Application for a certificate shall be made in writing to the Board and shall be so verified, shall be in such form and contain such information, and shall be accompanied by such proof of service upon interested persons, as the Board shall by regulation require.

Notice of Application

(c) Upon the filing of any such application, the Board shall give due notice thereof to the public by posting a notice of such application in the office of the secretary of the Board and to such other persons as the Board may by regulation determine. Any interested person may file with the Board a protest or memorandum of opposition to or in support of the issuance of a certificate. Such application shall be set for a public hearing, and the Board shall dispose of such application as speedily as possible.

Issuance of Certificate

(d)(1) The Board shall issue a certificate authorizing the whole or any part of the transportation covered by the application, if it finds that the applicant is fit, willing, and able to perform such transportation properly, and to conform to the provisions of this Act and the rules, regulations, and requirements of the Board hereunder, and that such transportation is required by the public convenience and necessity; otherwise such application shall be denied.

* * * * *

RATES FOR TRANSPORTATION OF MAIL

* * * * *

Sec. 406. [72 Stat. 763, as amended by 76 Stat. 145, 49 U.S.C. 1376]

* * * * *

Rate making elements

(b) In fixing and determining fair and reasonable rates of compensation under this section, the Board, considering the conditions peculiar to transportation by aircraft and to the particular air carrier or class of air carriers, may fix different rates for different air carriers or classes of air carriers, and different classes of service. In determining the rate in each case, the Board shall take into consideration, among other factors, (1) the condition that such air carriers may hold and operate under certificates authorizing the carriage of mail only by providing necessary and adequate facilities and service for the transportation of mail; (2) such standards respecting the character and quality of service to be rendered by air carriers as may be prescribed by or pursuant to law; and (3) the need of each such air carrier (other than a supplemental air carrier) for compensation for the transportation of mail sufficient to insure the performance of such service, and, together with all other revenue of the air carrier, to enable such air carrier under honest, economical, and efficient management, to maintain and continue the development of air transportation to the extent and of the character and quality required for the commerce of the United States, the Postal Service, and the national defense.

CLASSIFICATION AND EXEMPTION OF CARRIERS

Classification

Sec. 416. [72 Stat. 771, 49 U.S.C. 1386] (a) The Board may from time to time establish such just and reasonable classifications or groups of air carriers for the purposes of this title as the nature of the services performed by such air carriers shall require; and such just and reasonable rules and regulations, pursuant to and consistent with the provisions of this title, to be observed by each such class or group, as the Board finds necessary in the public interest.

Exemptions

(b)(1) The Board, from time to time and to the extent necessary, may (except as provided in paragraph (2) of this subsection) exempt from the requirements of this title or any provision thereof, or any rule, regulation, term, condition, or limitation prescribed thereunder, any air carrier or class of air carriers, if it finds that the enforcement of this title or such provision, or such rule, regulation, term, condition, or limitation is or would be an undue burden on such air carrier or class of air carriers by reason of the limited extent of, or unusual circumstances affecting, the operations of such air carrier or class of air carriers and is not in the public interest.

* * * * *

TITLE X--PROCEDURE

* * * * *

JUDICIAL REVIEW OF ORDERS

* * * * *

Sec. 1006. [72 Stat. 795, 49 U.S.C. 1486]

* * * * *

Findings of Fact Conclusive

(a) The findings of facts by the Board or Administrator, if supported by substantial evidence, shall be conclusive. No objection to an order of the Board or Administrator shall be considered by the court unless such objection shall have been urged before the Board or Administrator or, if it was not so urged, unless there were reasonable grounds for failure to do so.

* * * * *

FEB 14 1967

IN THE
United States Court of Appeals
FOR THE NINTH CIRCUIT

No. 20552

ISLAND AIRLINES, INCORPORATED, *Petitioner,*

v.

CIVIL AERONAUTICS BOARD, *Respondent.*

PETITIONER'S REPLY BRIEF

GEORGE F. GALLAND

G. NATHAN CALKINS

AMY SCUPI

GALLAND, KHARASCH, CALKINS
& LIPPMAN

1824 R Street, N. W.

Washington, D. C. 20009

Attorneys for Petitioner

April 12, 1966



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PETITIONER'S REPLY BRIEF

A. THE CLAIM OF RES JUDICATA

The CAB brief rests first (and apparently foremost) on the contention that the pending issues have been decided by this Court's decision in *Island Airlines, Inc. v. Civil Aeronautics Board*, 352 F. 2d 735 (1965). Under that case, this one is claimed to be *res judicata*, or barred by way of collateral estoppel (CAB Br., 8-10). The cited props for this argument are *Sunshine Anthracite Coal Co. v. Adkins*, 310 U.S. 381 (1940) and *Commissioner of Internal Revenue v. Sunnen*, 333 U.S. 591 (1948).

The question in *Adkins* was merely whether two government agencies were so far identical that a judgment against

the plaintiff in a suit involving one agency barred the same plaintiff from re-litigating the same point in a new action against the second. The answer: Yes. The case has no meaning here since we concede that the appellant and respondent in this case are the same as in the earlier one.

Sunnen holds the reverse of what the CAB seeks to prove by it. The question was whether a Tax Court decision involving royalty contracts which generated income in particular years was binding as to other, but identical, contracts of the same taxpayer in later years. The answer: No. The Court held that *res judicata* applies only to repetitious suits "involving the same cause of action," and continued (597, 599-600, 602):

"But where the second action between the same parties is upon a different cause or demand, the principle of *res judicata* is applied much more narrowly. In this situation, the judgment in the prior action operates as an estoppel, not as to matters which might have been litigated and determined, but 'only as to those matters in issue or points controverted, upon the determination of which the finding or verdict was rendered.' [Citations] Since the cause of action involved in the second proceeding is not swallowed by the judgment in the prior suit, the parties are free to litigate points which were not at issue in the first proceeding, even though such points might have been tendered and decided at that time. But matters which were actually litigated and determined in the first proceeding cannot later be relitigated. Once a party has fought out a matter in litigation with the other party, he cannot later renew that duel. In this sense, *res judicata* is usually and more accurately referred to as estoppel by judgment, or collateral estoppel."

* * * * *

"[Collateral estoppel] must be confined to situations where the matter raised in the second suit is identical in all respects with that decided in the first proceeding and where the controlling facts and applicable legal rules remain unchanged. [Citation] If the legal matters determined in the earlier case differ from those

raised in the second case, collateral estoppel has no bearing on the situation.”

* * * * *

“For income tax purposes, what is decided as to one contract is not conclusive as to any other contract which is not then in issue, however similar or identical it may be.”

In terms of the *Sunnen* test, neither *res judicata* nor collateral estoppel bars, or can be stretched to bar, the present appeal. At issue here is the question whether the CAB wrongly refused a requested exemption. That question never has been and never could have been previously decided because no exemption had been sought prior to the CAB proceeding which terminated in the order now under review.

The First *Island* case came to this Court from the District Court for Hawaii. *Civil Aeronautics Board v. Island Airlines, Inc.*, 235 F. Supp. 990 (1964). The Opinion narrates the scope and history of the case, revealing that:

1. Island inaugurated intra-Hawaii interisland service in 1963 under a rate order of the Hawaii Public Utilities Commission but without a CAB certificate. The PUC order was upheld by the Supreme Court of Hawaii (See 235 F. Supp. at 991-93).
2. The CAB sued Island in the District Court for an injunction against continuance of Island's interisland service without a CAB certificate. The CAB claimed exclusive jurisdiction on the ground that inter-island flights were impossible “without passing through air space over a place outside the state . . .” (235 F. Supp. at 992).
3. The injunction based on the decision at 235 F. Supp. 990 was preceded by one which this Court had set aside for failure of the District Court to find explicitly

the boundaries of Hawaii. This Court described the boundary question as the "root of the problem." *Island Airlines, Inc. v. Civil Aeronautics Board*, 331 F. 2d at 207, 208 (1964). The reason for requiring vacation of the injunction was that the injunction implied the international status of the inter-island channels, thereby raising "a constitutional question of equal protection of the laws, something traditionally avoided by the courts, if there be a non-constitutional basis for decision" (331 F. 2d at 208).

4. On remand, the District Court (a) found explicitly that the interisland channels were international, and (b) reinstated its injunction. It twice characterized the boundary question as the *only* issue in the case, stating (235 F. Supp. at 993):

"... no problem is presented other than the determination by this court whether Island is carrying on air transportation in violation of Section 401 (a) of the Act."

* * *

"The evidence and argument presented before this court thereafter, [i.e., after remand] was almost entirely confined to 'the root of the problem ... [viz.] where is the boundary or boundaries of the state of Hawaii?'"

5. The District Court held that Hawaii was not demoted to second-class statehood or deprived of equal footing by reason of Congressional omission to give the state control of the interisland passages (235 F. Supp. at 1007-8).
6. Having determined that the State of Hawaii did not include the interisland channels, the District Court held that the international channels were a "place" outside Hawaii under Section 101(21)(a) of the Federal Aviation Act (235 F. Supp. at 994).

In affirming the District Court, this Court summarized Island's contentions on appeal in these terms (352 F. 2d at 738-9):

- “(1) The boundaries of a state are determined by Congress, not international law. Congress, by the Hawaiian Statehood Act, established the ‘channels’ between the Hawaiian Islands as being within the boundaries of the State of Hawaii. And even if we assume the enjoined flights pass over international waters subject to no sovereignty, such waters are not ‘a place’ within the statute defining ‘interstate air transportation.’ (49 U.S.C. § 1301 (21)(a).)
- (2) The federal courts (a) should have abstained from exercising jurisdiction; (b) the federal courts had no jurisdiction; and (c) the State of Hawaii was an indispensable party.
- (3) Certain findings as to flight patterns and effect on subsidies are without evidentiary support.”¹

This Court's opinion addressed itself primarily to the first of these contentions, agreeing with the Court below as to State boundaries and the status of interisland waters as a “place”. It also dealt briefly but explicitly with the constitutional question foreshadowed in its first opinion, stating (352 F. 2d at 744):

“We find no ‘invidious discrimination’ against the State of Hawaii in the court's decision below. ‘Equal boundaries to each state are not necessary.’ *United States v. Louisiana*, 363 U.S. 1, 77.”

It is thus clear that this Court's only constitutional ruling was that the Hawaii Admission Act was not unconstitutional in failing to award the open seas between the islands to the new State—and Island claims nothing to the contrary in this proceeding. On the basis of the constitu-

¹ A fourth contention had to do with a counterclaim not here relevant.

tional ruling that the islands of Hawaii were separated by international waters, it held that the Federal Aviation Act applied to interisland transportation in accordance with the Act's explicit terms—and Island claims nothing to the contrary in this proceeding.²

Island's uncertificated operations and its resistance to the CAB injunction proceedings against them rested on the view that the Federal Aviation Act did not cover interisland flights because Hawaii was, from end to end, a geographical unit. This Court held that the Act *does* apply, since the State is *not* a geographical unit. The decision that the Act applies means that the whole Act applies; and since the whole Act contains an exemption provision, the decision validates that provision as clearly and completely as it validated the certification requirement.

This Court's decision that the Act covers Island's operations necessarily means that a certificate is needed unless the CAB grants an exemption, because that is what the Act says. The decision means nothing as to whether an exemption should be granted, because none was ever before sought. The *res judicata* contention of the CAB omits to note that (a) the earlier case was a constitutional contro-

² This Court expressed its general conclusion thus (352 F. 2d at 742):

"If the flights are intrastate, then of course, the federal courts should not permit the C.A.B. to require a certificate, but conversely, if the 'channels' are high seas, then flight over them should and must be subject to the C.A.B.'s authority. This general principle of the supremacy of federal control over interstate and high seas flights must prevail, *if the facts support it*, over the paramount importance to the Hawaiian economy of inter-island air transportation." (Italics added)

While the District Court discussed some operational and economic matters (235 F. Supp. at 1008) which it thought to favor national over local regulation, this Court brushed such pronouncements aside as mere "make weight" (325 F. 2d at 744). As this Court noted in the first Island appeal, the case lacks "anything to do with safety—a function of the Federal Aviation Authority. The sweep of the decree in its present form could only be sustained on the basis that the intervening seas (less offshore limits) are no part of the State of Hawaii." (331 F. 2d at 208)

versy over the scope and validity of the Hawaii Admission Act, whereas (b) this case presents issues of administrative law involving the propriety of agency conduct under the Federal Aviation Act. The two problems are palpably discrete.

The CAB asserts (CAB Br., 10) that "there has been neither change in the dispositive facts nor any intervening legal development" since the injunction suit. That assertion ignores the exemption application which is the whole fabric of this case. No question bearing on exemption (or on any other administrative power of the CAB) was "considered less than six months ago" or "decided adversely to Island" because no such question was considered or decided ever—for the reason that no such question had ever arisen.

B. ABUSE OF DISCRETION

1. Non-Responsiveness of the Board's Brief

The CAB Brief seems to us almost systematically non-responsive to the Island presentation. Island's case for exemption was tendered to the CAB as a basic problem of federalism, involving the most sensitive of political subjects, viz: the distribution of sovereign power between a state government and the national government.³

We contended in our opening brief that the Board in denying exemption had ignored the applicable constitutional and administrative principles and failed either to find or heed the facts necessary to guide it in the application of such principles. Its brief is a repetition and amplification of the same errors. Nowhere between its covers does the brief offer a hint of recognition of Hawaii's accession to statehood; of the bearing of that event on the Board's administrative obligations; of the State's declared need for economical air service; of its unique geography; of its isolated

³ Island Opening Brief, 9-11, 14-33.

position; of the shortcomings of existing carriers; of those carriers' boasts of monopoly; of their failure to meet relevant criteria of convenience and necessity; or of any circumstance beyond the unsupported grumble of Aloha and Hawaii that competition will cost them patronage and boost the level of federal subsidy. We submit that the Board's conduct constitutes a plain abdication of official duty.

2. The Exemption Power—Judicial Authorities

Besides declining to debate, the Board seeks protection behind a flurry of citations which either do it no good or much harm. For the proposition that Island misconceives the nature of exemption, the Board cites (CAB Br., 13) *United Air Lines, Inc. v. Civil Aeronautics Board*, 278 F. 2d 446 (D.C. Cir., 1960),⁴ *American Airlines v. Civil Aeronautics Board*, 235 F. 2d 845 (D.C. Cir., 1956), and *Pan American World Airways v. Civil Aeronautics Board*, 261 F. 2d 754 (D.C. Cir., 1958), cert. denied, 359 U.S. 912 (1959).

What *United* held as to exemption was (278 F. 2d at 449):

“We do not have before us exemption authority under Section 416 of the Act and so express no opinion on that matter.”

If the Court had expressed an opinion, its precedential value would have declined observably when the Supreme Court vacated the judgment *sub nom. All American Airways, Inc. v. United Air Lines*, 364 U.S. 297 (1960).

American Airlines was cited by Island (Island Opening Brief, 6) for the proposition that orders in exemption cases must be supported by adequate findings. The order in *American* was so broad that it evoked assault by two printed columns of appellants comprising virtually the whole network of the country's major airlines plus a railroad for good measure (235 F. 2d at 845). Despite the

⁴ Mis-cited by the Board as 279 F. 2d.

breadth of the exemption order—which permitted 49 nationwide air carriers to make 10 flights a month each between any pair of points—the Court held that the order was within the Board’s competence *if supported by proper findings* (235 F. 2d at 851). Only for the lack of such findings was the exemption set aside; and only for the same reason did the Court invalidate the exemption order involved in *Pan American*.

3. The Board’s View of the Public Interest

The CAB brief, like the order under review, reflects throughout an obsessive concern for the protection of Aloha and Hawaiian against competition, and equates such protection with the public interest without revealing what public, or what interest of such public, is the object of the Board’s fierce paternalism. The Board’s attitude is a puzzlement in view of the disparity between its own prejudices and the strongly conflicting views of the Hawaii Government. The State (as a state, in distinction to a territory) has unquestioned authority as *parens patriae*, to voice the transportation needs of its citizens and to seek their federal recognition. *Georgia v. Pennsylvania R.R. Co.*, 324 U.S. 439 (1945). There the Court said:

“Georgia as a representative of the public is complaining of a wrong, which if proven, limits the opportunities of her people, shackles her industries, retards her development, and relegates her to an inferior economic position among her sister States. These are matters of grave public concern in which Georgia has an interest apart from that of particular individuals who may be affected. Georgia’s interest is not remote; it is immediate.” (324 U.S. at 451).

In its capacity of *parens patriae*, Hawaii represented to the CAB and represents to this Court that the public interest calls for a state-regulated economy-type service in addition to the services of Aloha and Hawaiian. We do not

claim that the CAB must take orders from Hawaii but we do elaim, and the cases prove, that it was obligated to resolve the issues which Hawaii tendered within the scope of this proceeding—which is precisely what the Board declines to do.

The Board (CAB Br., 14) adopts the test whether Island's service will "unduly impinge on the certificated system"—concluding without inquiry that it will; and reminds the Court (CAB Br., 18) that the agency "customarily takes into consideration the competitive impact . . . upon existing carriers operating pursuant to certificates of public convenience and necessity"—thereupon reflexively delegating its veto to Aloha and Hawaiian.

We do not see how the Board can decide whether "impingement" is "undue" without at least trying (a) to gauge its effect and (b) to appraise the standing and performance of the entrenched certificate-holders. It made no move in either direction but would have absorbed some meaningful learning had it done so.

As to the effect of "impingement", the Board could have learned from its own published study (annexed to Island's Opening Brief as Appendix B) that competition can stimulate the moribund, to their great (if unwanted) advantage.⁵ If it did not wish to look so far, it had only to read its own decision on the certification of Aloha (then called Transpacific), for convincing proof that Aloha's competition would *and did* help Hawaiian to increase its

⁵ The Board now recoils from this study (CAB Br., 22) because it does "not necessarily reflect the official views or opinions of the Board Members themselves" and because it was only designed "to throw light on the factors generating air passenger traffic." We are intrigued by the unique practice of coyly issuing official documents so that the public can try to guess whether the Board thinks that they mean what they say. We submit that unless the figures in the study are false, they fulfill brilliantly their mission of casting light on the relationship between competition and passenger volume.

passengers and revenues. *Hawaiian Intraterritorial Service*, 10 C.A.B. 62, 66, 78-79 (1948).⁶

The same case qualifies in substantial measure the implications of the Board's statement here (CAB Br., 20) that "Hawaiian and Aloha, both operating pursuant to certificates issued by the Board, are part of the national air transportation system."

As has been noted (Island Opening Brief, 13-14), Hawaiian and Aloha were both certificated before statehood. Hawaiian received a grandfather certificate (CAB Br., 3, n. 3) on proof of nothing whatever except early arrival on the scene. Aloha was certificated later (10 C.A.B. 62) on the ground that Hawaiian's monopoly was bad for the territory (10 C.A.B. at 65). The Board found that Aloha had recurrently violated the Civil Aeronautics Act and would be unfit for certification under normal standards, but would be certified nevertheless because no other monopoly-breaker was at hand (10 C.A.B. at 67). The Board, finding need

⁶ "The provision for a second or alternative service for an area almost wholly dependent on air transportation is not the sole benefit which would be derived from granting a certificate of public convenience and necessity to Trans-Pacific. The award would have the incidental advantage of providing a competitive spur to Hawaiian, and of assuring the continuation of improved services which may have been instituted by Hawaiian as a result of the service of the noncertificated carriers. The record shows that, about the time Trans-Pacific and other non-scheduled air carriers started service, Hawaiian instituted a number of improvements in its service. Thus, in the summer of 1946 it began to make use of travel bureaus, and also provided additional, and in many instances more convenient, ticket facilities for the traveling public. In the spring of 1946 Hawaiian reduced fares to an average of 6.5 cents per mile and also expanded its facilities and obtained additional aircraft. In February 1948, a few weeks after Trans-Pacific discontinued all common-carrier operations, Hawaiian raised fares to yield 7.5 cents per revenue passenger mile, an increase of approximately 15 percent. Whether this increase was a coincidence or a result of the termination of Trans-Pacific's operations, the foregoing are examples of improvements in service which take place under the stimulus of competition. *It should be noted also that during the period Hawaiian was operating under the lower fares, its operating revenues were increasing over the corresponding period in previous years.*" (10 C.A.B. at 66). (Italics added.)

to scrape the bottom of the barrel, dutifully braced itself and scraped—and came up with the Aloha certificate.⁷

These conditions of certification of Aloha and Hawaiian detract from the protective lustre that more conventionally-earned certificates normally carry. Not only do the facts negate the usual implications of public convenience and necessity, and of fitness, willingness, and ability to perform, but quite as importantly, they refute the Board's assertion that the two carriers are part of the national transportation system.

The case which brought forth Aloha's certificate was concluded in 1948 while Hawaii was a territory with thirteen years to go before statehood. The title of the case was *Hawaiian Intraterritorial Service*. The first sentence of the Report (10 C.A.B. 62) states: "In this proceeding the Board is considering the air transportation needs of the Territory of Hawaii." The reasons given for providing additional service within the territory had nothing to do with any relationship to a national transportation system: rather, they took account of the "great distance" between Hawaii and the mainland which forced most Hawaiians who travelled at all to travel *within* the territory (10 C.A.B. at 77). Thus, the interisland carriers were recognized not as a part of the national transport system but as carriers whose existence was justified because they were outside of such system. Certainly a service which was "local" under territorial status does not become national under statehood.

We are not, of course (as the CAB implies we are—CAB Br., 22, n. 22) seeking decertification of Aloha or Hawaiian. We are urging that in view of the conditions of certification, neither certificate confers automatic and ever-

⁷ The Board said: "We do not intend to reward wrongdoers by granting certificates . . ." (10 C.A.B. at 67), and granted the wrongdoer a certificate.

lasting immunity, on grounds of public interest, against future competition. In summary, our position is:

1. Hawaiian received a grandfather certificate.
2. On certification, Hawaiian became a monopolist whose monopoly the CAB pronounced detrimental to the public interest.
3. To break the monopoly, the CAB certified Aloha despite a finding of unfitness under normal criteria.
4. Neither carrier was certified as a part of the national air transportation system but merely as a local carrier in an isolated federal territory.
5. Neither Aloha nor Hawaiian has passed the tests by which they would be judged in seeking certification after Hawaii's accession to statehood.

The CAB not only persists in forecasting (contrary to relevant indicators) loss of revenue to Aloha and Hawaiian if they encounter competition, but an automatic increase in federal subsidy to offset the decline. Surely the law calls for no such fiscal extravaganza. If Island survives on low fares and no subsidy, it will be proving not that the Aloha and Hawaiian subsidies must be boosted but that they should be dropped. No sane conception of public interest demands that there must always be a subsidy, or a supplicant to claim it. In any event, the CAB has not attempted to refute our legal demonstration (Island Opening Brief, 23-25) that a vital state police power cannot be negated for the sake of pinching federal pennies.⁸

4. Hawaiian Statehood

The CAB Brief (CAB Br., 5, 15-22) incorrectly interprets the history of the Hawaii Statehood Act as proof that Congress meant to keep interisland air transportation

⁸ The District Court's observations on the relationship between competition and subsidy (235 F. Supp. at 1009) were beyond the issues in the injunction suit, and were not adopted by this Court on appeal.

“subject to economic regulation *by the Board.*” The Senate Committee on Insular Affairs reported merely that “the provisions of the Federal Aviation Act . . . should continue in accordance with the definition of interstate air transportation as contained in that Act.”⁹ The Committee was reporting only the Hawaiian Statehood Act (Pub. Law 86-3, 73 Stat. 4). The Statehood Act embodied no amendment to the Federal Aviation Act and thus could not have changed its meaning. The Statehood Act in Section 18 *did* refer explicitly to the Interstate Commerce Act and the Shipping Act as regards their application to Hawaiian commerce. Its references to those statutes while omitting any reference to the Federal Aviation Act reinforces the natural conclusion that the Aviation Act remained in *status quo*. Accordingly, Hawaiian interisland commerce remained under the Federal Aviation Act (as it would had the Committee remained silent)—but not inevitably subject to regulation by the Civil Aeronautics Board—because the Act provides a system for the granting of exemptions. Nothing in the Statehood Act curtails the use of the exemption mechanism.

While the injunction litigation affirmed the constitutionality of the Statehood Act and the consequent applicability of the Federal Aviation Act, it went no further.¹⁰ It neither conferred nor implied a license for the CAB capriciously to strip Hawaii of a vital State power without necessity, or to ignore an urgent local condition as an element of the public interest. This Court held on the injunction appeal

⁹ S. Rep. No. 80, 86th Cong., 1st Sess. (1959).

¹⁰ Even the basis for applicability of the Federal Aviation Act to Hawaiian interisland transportation remains obscure. As Island has shown (Island Opening Brief, 18, n. 21), such transportation involves “commerce with foreign nations” under *Lord v. Goodall*, 102 U.S. 541 (1881), whereas it is “interstate” under the Act. The discrepancy evidently troubled the District Judge in the injunction suit, since in quoting from *Lord*, he substituted asterisks for the words “with foreign nations”—leaving the San Francisco-San Diego Voyage characterized merely as “commerce * * * ” (235 F. Supp. at 995).

that the general principle of federal supremacy must control "if the facts support it". (352 F. 2d at 742). The exemption petition reviews the facts and demonstrates that this is one instance where federal authority should accede to state control. When Hawaii became a state, it acquired the full range of prerogatives of all other states, including the right to have the Federal Government forbear from heedless intrusion into local affairs.¹¹ Even if the Congress could constitutionally preempt the power of regulating interisland commerce, the CAB cannot claim equally wide-ranging authority in the absence of sound reason for its action. It is subject, as Congress is not, to a broad spectrum of administrative restraints. Among them, we submit, is a restraint against usurpation of state power to solve a state problem when the usurpation serves no serious federal objective.¹² But except as it seeks cover behind this Court's previous *Island* decision (CAB Br., 15, 24), the Board never comes to grips with the question as to how the separation of Hawaii's island areas by patches of open

¹¹ Island Opening Brief, 15-17.

¹² The position of Hawaii as spokesman for its citizens is analogous to that of the citizen protestants in *Office of Communication of the United Church of Christ v. Federal Communications Commission*, F. 2d (D. C. Cir., March 25, 1966). The FCC had denied such protestants standing as parties. The Court of Appeals reversed, stating (slip opinion, 17, 22):

"... unless the listeners—the broadcast consumers—can be heard, there may be no one to bring programming deficiencies or offensive overcommercialization to the attention of the Commission in an effective manner."

* * *

"When past performance is in conflict with the public interest, a very heavy burden rests on the renewal applicant to show how a renewal can be reconciled with the public interest. Like public officials charged with a public trust, a renewal applicant, as we noted in our discussion of standing, must literally 'run on his record.' "

While Aloha and Hawaiian have nothing before the CAB for renewal, the exemption application inherently tests their continuing right to shut out competition on the basis of stale certificates granted under superseded conditions. When they seek to perpetuate their monopoly, they should be required to "run on their record" as the Court required of the renewal applicant in the case cited.

sea diminishes Hawaii's interest, as compared to other states, in seeking to meet local transportation needs. In its brief, the Board asserts that this Court's adjudication in the injunction case prohibits the grant of exemption. Thus the brief is a clear admission that the petition was never seriously considered by the Board, because the Board felt that under the earlier decision, federal control of Hawaiian intrastate commerce was mandatory. On this basis alone, the case merits reversal.¹³

The Board's brief, compressed to its essentials, is an argument that a subsidized air line (in Hawaii only) must never be exposed to business forces which will either (a) increase its subsidy need (by taking cargo), or (b) diminish such need (by spurring efficiency). We find nothing in the Board's position more constructive than a droning insistence that whatever impinges on a ward of the agency is contrary to the public interest. For a conflicting view, urging the need to emphasize state responsibility and to de-emphasize subsidy, we refer to President Kennedy's Special Transportation message to the Congress, excerpted in the Appendix to this Brief.

5. Residual Matters

The Board hints darkly that if the State succeeds to regulatory control under a federal exemption, a limitless flood of new carriers will choke Hawaii's airways and bankrupt the industry (CAB Br., 19, 23). This could occur only if both Hawaii and the CAB abdicated their duties. As to

¹³ We have shown that no court decision and no congressional action has foreclosed the exemption issue. We again invite to this Court's attention the memoranda appended to the Senate Report on the Statehood Bill (S. Rep. No. 80, 86th Cong., 1st Sess., App. F (1959)), showing the virtual absence of federal interest in intra-Hawaiian interisland commerce (Island Opening Brief, 10). A further congressional expression that the islands of Hawaii are not to be treated as separate states is the provision in Public Law 86-661, 74 Stat. 527. That enactment authorized temporary certification of various supplemental air carriers and provided that for the purposes of the Act, "the State of Hawaii shall be considered one point."

Hawaii, we see no reason why it should regulate less wisely than California, under whose supervision Pacific Southwest Airlines has flourished to the point of evoking a CAB accolade. (Island Opening Brief, App. B). The Board could, indeed, condition an interisland exemption on the continuance of regulatory control by Hawaii, just as it has done in the case of intra-Alaskan air taxis, 14 C.F.R. 298.21(c). Under the cited regulation, the exemption of such taxis (also those in Alaska-Canada service) is expressly conditioned on their holding authority from Alaska. Thus has the Board worked out an accommodation with a state by transfer to the state of a congressionally-delegated function, in a constructive demonstration of pragmatic federalism.

C. PROOF AND PROCEDURE

The Board charges Island with an impressive succession of procedural shortcomings: (1) failure to set forth enough economic data in its application (CAB Br., 18-19); (2) failure to deny the answers of Aloha and Hawaiian (CAB Br., 25); and (3) failure to request a hearing (CAB Br., 11, 25). We consider these matters in order.

1. Factual Content of the Application

We are not sure where the Board feels that we fell short under this heading. Its emphasis on absence of "facts or supporting data" (CAB Br., 18) implies that Island should have filed and proved a certification case rather than an exemption application. Island, however, was entitled to elect, as it did elect, the type of relief to pursue and its petition met fully the requirement of the applicable rule (CAB Br., 18 n. 18). Under that rule, an exemption petition may comprise two types of material: (a) facts to be noticed officially, and (b) "affidavits establishing such other facts as the applicant desires the Board to rely upon" (14 C.F.R. 302.402(c)).

The basis of the claimed exemption was a set of constitutional, political and geographic relationships which are standard targets of official notice, coupled with basic facts as to the identity and activities of the parties which are matters of official record. Statistical minutiae were no part of Island's case and have no proper place in its petition, which reveals all that needs revelation as to public interest, undue burden, unusual circumstances, and other pertinent criteria.

2. Failure To Controvert Answers

Island's reasons for not replying to the answers were that (a) they were not responsive to the petition, and (b) they consisted of unsubstantiated allegations, conclusions and arguments (not evidence) to which no reply was necessary.

We repeat that the proceeding inaugurated by Island's petition was *not* an application for a certificate of public convenience and necessity, and neither the interveners nor the Board had authority to transmute it into one. The answers treated the petition as if it were such an application. To hold Island accountable for contesting allegations as to public convenience and necessity would mean that interveners have the power to bait an applicant into the waging of a battle it never entered.

Moreover, the Aloha and Hawaiian answers did not, in their material assertions, satisfy the Board's rule for consideration as evidence. The rule requires (14 CFR 302.406) that answers, like petitions, include (a) material officially noticeable; and (b) affidavits, of which none were submitted. Perhaps some of the interveners' statistical tables could be noticed officially but certainly the interveners' conclusory assertions on which the Board based its decision could not. A statement that "a third carrier competing on these routes would be disastrous" (R. 44) or "the Island charge that the certificated carriers cater to

the carriage trade is baseless" (R. 45) would not be evidence no matter how many oaths supported them; much less are they evidence when bandied about (as they were here) in a lawyer's brief. *Minnesota Rate Cases*, 230 U.S. 352, 33 S. Ct. 729, 767 (1913). This however, was the type of evidence on which the Board found in its order that the Federal Government's interest in Aloha and Hawaiian "could be adversely affected by the exemption requested;" that "Aloha estimates that Island's proposed service would divert \$1,000,000 annual revenue;" that "Hawaiian estimates that the two subsidized carriers would lose an additional \$4,856,000 annually." (R. 168(a)).

Denials of such "evidence" are not only unnecessary but futile: the Board found no facts, but only that Aloha and Hawaiian "estimate" various frightful eventualities. We may assume realistically that such estimates would not be abandoned or altered no matter how vociferously denied. Fortune-telling is not subject to the rules of common-law pleading.

3. Omission To Demand Hearing

Island did not demand a hearing because the facts on which it relied were officially noticeable and needed no further proof. It was under no obligation to demand a hearing for the purpose of enabling the interveners to establish their unproved assertions. Neither was it obliged to demand a hearing in order to disprove facts never proved by their proponents.

We contended in our opening brief that some form of procedural due process was needed before the Board could resolve the case against Island on unsustained assertions of its opponents. One case we cited (Island Opening Brief, 37) was *First National Bank of Smithfield v. First National Bank of E.N.C.*, 232 F. Supp. 725 (E.D.N.C., 1964). That case, as the Board noted, now stands reversed. *First National Bank of Smithfield v. Saxon*, 352 F. 2d 267 (4th Cir.,

1965). The reversal was first noted by *Shepard's Citations* after the Island brief was written.

The reversing decision merits attention on two counts: (a) it involved a 2-1 division, with a strong and arresting dissent by Judge Sobeloff (352 F. 2d at 273); and (b) the majority opinion dealt more harshly with the authority whose action was under review than did the decision of the District Court. The District Court had held that the Comptroller of the Currency had been obliged to hold a hearing on a request for a branch banking permit. The Court of Appeals ruled a hearing unnecessary. In so ruling, however, it held that a comptroller's finding reached after hearing would be reversal-proof if supported by substantial evidence, whereas a finding made without a hearing would be replaced *by a finding of the court after a trial de novo*. The reversal, we submit, justifies this Court in reaching its own decision on the Island exemption application without remand to the CAB.

Respectfully submitted,

GEORGE F. GALLAND

G. NATHAN CALKINS

AMY SCUPI

GALLAND, KHARASCH, CALKINS
& LIPPMAN

1824 R Street, N. W.

Washington, D. C. 20009

Attorneys for Petitioner

April 12, 1966

APPENDIX

On April 5th, 1962, the President sent to Congress a special message discussing "an efficient transportation system".¹⁴ The philosophy therein expressed differs markedly from that set forth in the CAB Brief. The following are quotations from this message (4148-49, 50, 55):

"No simple Federal solution can end the problems of any particular company or mode of transportation. On the contrary, I am convinced that less Federal Regulation and subsidization is in the long run a prime prerequisite of a healthy intercity transportation network.

The constructive efforts of State and local governments as well as the transportation industry will also be needed to revitalize our transportation services."

* * *

"This basic objective can and must be achieved primarily by continued reliance on unsubsidized privately owned facilities, operating under the incentives of private profit and the checks of competition to the maximum extent practicable. The role of public policy should be to provide a consistent and comprehensive framework of equal competitive opportunity that will achieve this objective at the lowest economic and social cost to the Nation.

This means a more coordinated Federal policy and a less segmented approach. It means equality of opportunity for all forms of transportation and their users and undue preference to none. It means greater reliance on the forces of competition and less reliance on the restraints of regulation."

* * *

"Our system of intercity public transportation—including railroads, trucks, buses, ships and barges, airplanes, and pipelines—is seriously weakened today by artificial distortions and inefficiencies inherent in existing Federal policies. Built up over the years, they can

¹⁴ U.S. Code Cong. and Ad. News, 87th Cong., 2d Sess., page 4148 (1962).

be removed only gradually if we are to mitigate the hardships that are bound to arise in any program of far-reaching adjustment."

* * *

"At my request, the problems of urban transportation have been studied in detail by the Housing and Home Finance Administrator and the Secretary of Commerce. Their field investigations have included some 40 metropolitan and other communities, large and small. Their findings support the need for substantial expansion and important changes in the urban mass transportation program authorized in the Housing Act of 1961 as well as revisions in Federal highway legislation. They give dramatic emphasis, moreover, to the need for greater local initiative and to the responsibility of the States and municipalities to provide financial support and effective governmental auspices for strengthening and improving urban transportation."

Iolani Palace Grounds
Honolulu, Hawaii

IN THE UNITED STATES COURT OF APPEALS
FOR THE NINTH CIRCUIT

ISLAND AIRLINES, INCORPORATED,)
)
) Petitioner,)
)
) vs.)
)
) CIVIL AERONAUTICS BOARD,)
)
) Respondent.)
)

BRIEF OF AMICUS CURIAE
STATE OF HAWAII

Pursuant to Rule 18 of this Court, STATE OF HAWAII files this Brief as amicus curiae in the above-entitled proceeding. The State of Hawaii still maintains that jurisdiction over inter-island common-carrier air transportation is properly vested in its Public Utilities Commission, as indicated in the opinion of its Supreme Court on June 21, 1963, In re Island Airlines, 47 Haw. 87, 384 P.2d 536. While the State of Hawaii feels bound on the jurisdictional issue so decided, it nonetheless recognizes that this Court recently rendered a contrary position in the injunction proceedings of Island Airlines, Inc. vs. C.A.B., 352 F.2d 735.

Without prejudice to its position on jurisdiction, the State of Hawaii files this Brief in order to clarify its position on two points:

(1) That it presently has the necessary law and machinery to properly regulate common-carrier air-transportation service between the islands, and

(2) That public need and necessity for such local service have been adequately demonstrated.

STATE OF HAWAII HAS THE NECESSARY
MACHINERY TO REGULATE INTER-ISLAND
AIR TRANSPORTATION

Since the enactment of the Public Utilities statute in 1913, the State of Hawaii has continuously regulated its public utilities. Its present Public Utilities Commission, consisting of five members, has provided needed meaningful regulation of all public utilities as defined in the statute on all islands. The Commissioners representing the major four islands of the Hawaiian group (Oahu, Hawaii, Maui and Kauai) have served efficiently on a part-time, staggered-term basis for nominal compensation.

This Commission has provided necessary regulation of rates, fares, charges, classification, rules and practices, financial transactions, securities and other regulatory matters dealing with public utilities corporations. It is

even now regulating the two inter-island air common carriers-- Hawaiian Airlines and Aloha Airlines--C.A.B. certified air carriers, in its issuance of securities and other financial transactions. Even before Hawaiian statehood, both air carriers sought prior approval of the Hawaiian Public Utilities Commission before issuance of stocks, certificates, bonds, notes and other evidence of indebtedness as required by State statutes.

LOCAL NEED HAS BEEN ADEQUATELY SHOWN

Since the initial application of Island Airlines filed before the Public Utilities Commission for approval of rates, fares, and schedules in early 1960, many public hearings on all major islands have been held. At these hearings need and necessity for a local inter-island low-cost common-carrier air-passenger service linking all islands in the Hawaiian group have been demonstrated. Almost all witnesses in testimony elicited during these five intermittent years of hearings on the Island Airlines' rate applications before the Public Utilities Commission have voiced strong support for and urged early approval of such service. The orderly development of a total State economy depends greatly on a local low-cost mass air-transportation

service. Such service will enable local residents to visit neighbors, friends and relatives on other islands, providing a major air thoroughfare for business and pleasure travel at economical rates.

The short history of Island Airlines' operation in spring, 1963, was marked by solid local support for such economical mass air-transportation service. Moreover, the surveys conducted before, during and after such service affirm the finding that more than half of all local residents have not visited other islands primarily because of cost considerations. These parties have voiced their desires to utilize and support a low-cost air common-carrier service if provided for local residents.

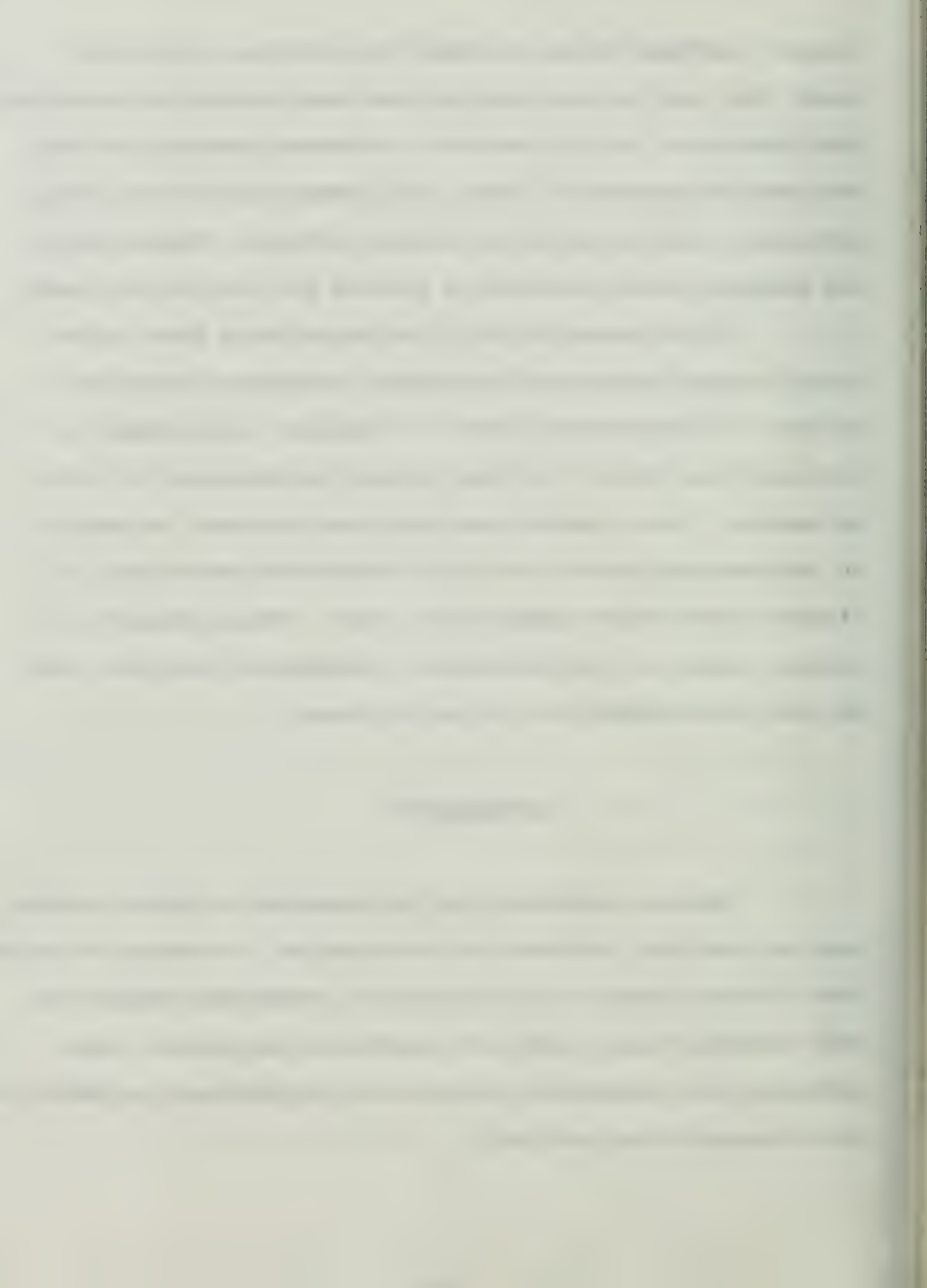
Decision and Order 1502 filed February 1, 1965, by the Hawaii Public Utilities Commission came after months of prolonged hearings, testimony and other evidence submitted by Island Airlines and the C.A.B. certified carriers--Hawaiian and Aloha Airlines. This authorization issued by the Commission on February 1, 1965, approving Island Airlines' proposed rates and charges authorized Island Airlines to operate on the proposed schedules and rates for a test period of one year beginning six months after the effective date of the order, or such extensions as the Commission might grant. The authorization to operate during the test period

clearly confined Island Airlines to providing a strictly local "Sky Bus" service and excluded any interstate operations. The Commission, in its decision, evidenced recognition that the need for economical local mass common-carrier air transportation would be served by Island Airlines, whereas Aloha and Hawaiian would continue to provide for the tourist needs.

Both houses of the State Legislature have, after study, passed concurrent resolutions requesting exemption by the Civil Aeronautics Board of Hawaiian intra-state air carriers from Title IV of the Federal Aviation Act of 1958, as amended. Said resolutions have been attached as exhibits in the hearings before the Civil Aeronautics Board and included in the record before this Court. These resolutions clearly point out the legislative findings of the local need to link the islands into one major State.

CONCLUSION

However competent and well-meaning a federal agency such as the Civil Aeronautics Board may be, it cannot be denied that a State agency acutely sensitive, aware and attuned to ever changing local needs and conditions can provide more effective and meaningful controls and regulations for Hawaii's air-transportation problems.



WHEREFORE, the State of Hawaii submits that if permitted, its Public Utilities Commission can, will and should properly regulate, enforce and control all economic regulations for local, intra-state common-carrier air service serving local needs and for local conditions.

DATED: Honolulu, Hawaii, February 28, 1966.

STATE OF HAWAII, Amicus Curiae
By BERT T. KOBAYASHI
Attorney General

By /s/ Arthur S. K. Fong
ARTHUR S. K. FONG
Deputy Attorney General



CERTIFICATE OF SERVICE

I hereby certify that I have this day served the foregoing document by depositing the same in the United States Post Office at Honolulu, Hawaii, properly addressed and postage prepaid to:

Mr. George F. Galland
Galland, Kharasch, Calkins & Lippman
1824 R Street, N.W.
Washington, D. C. 20009

Mr. Kenneth F. C. Char, President
Aloha Airlines, Inc.
Honolulu International Airport
Honolulu, Hawaii 96819

Mr. Jack Magoon, President
Hawaiian Airlines
Honolulu International Airport
Honolulu, Hawaii 96819

Civil Aeronautics Board
Washington, D. C. 20428

DATED: Honolulu, Hawaii, March 4th, 1966.

/s/ Arthur S. K. Fong

ARTHUR S. K. FONG

FEB 14 1967

No. 20552

IN THE UNITED STATES COURT OF APPEALS

FOR THE NINTH CIRCUIT

ISLAND AIRLINES, INCORPORATED,)

Petitioner,)

vs.)

CIVIL AERONAUTICS BOARD,)

Respondent.)

PETITION TO REVIEW
ORDER OF THE CIVIL
AERONAUTICS BOARD

BRIEF FOR ALOHA AIRLINES, INC.,
AMICUS CURIAE

FILED

APR 13 1966

WM. E. LUCK, CLERK

J. RUSSELL CADES
WILLIAM M. SWOPE
165 South King Street
Honolulu, Hawaii

Attorneys for Aloha Airlines,
Inc., Amicus Curiae

Of Counsel:

SMITH, WILD, BEEBE & CADES

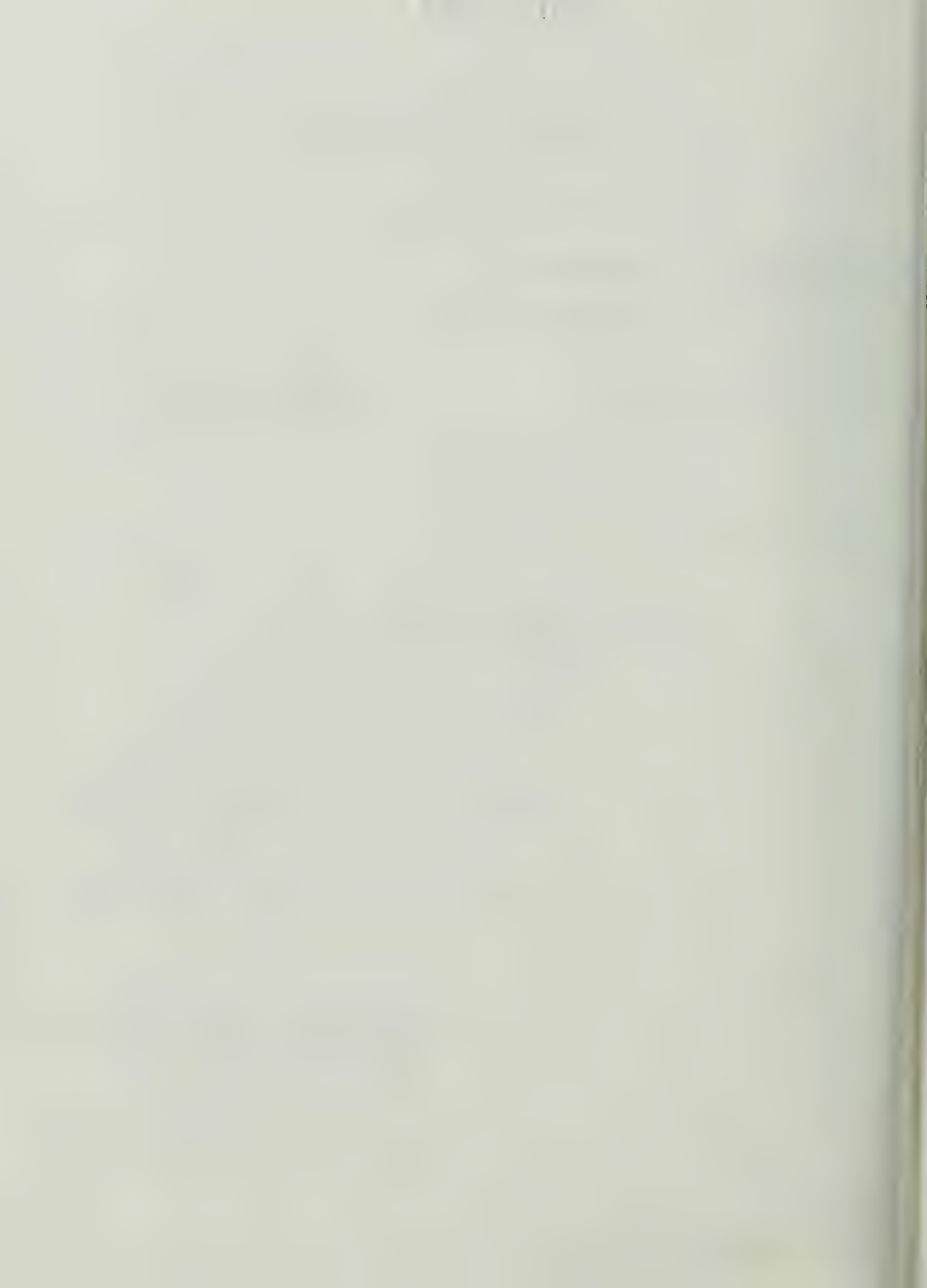


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No. 20552

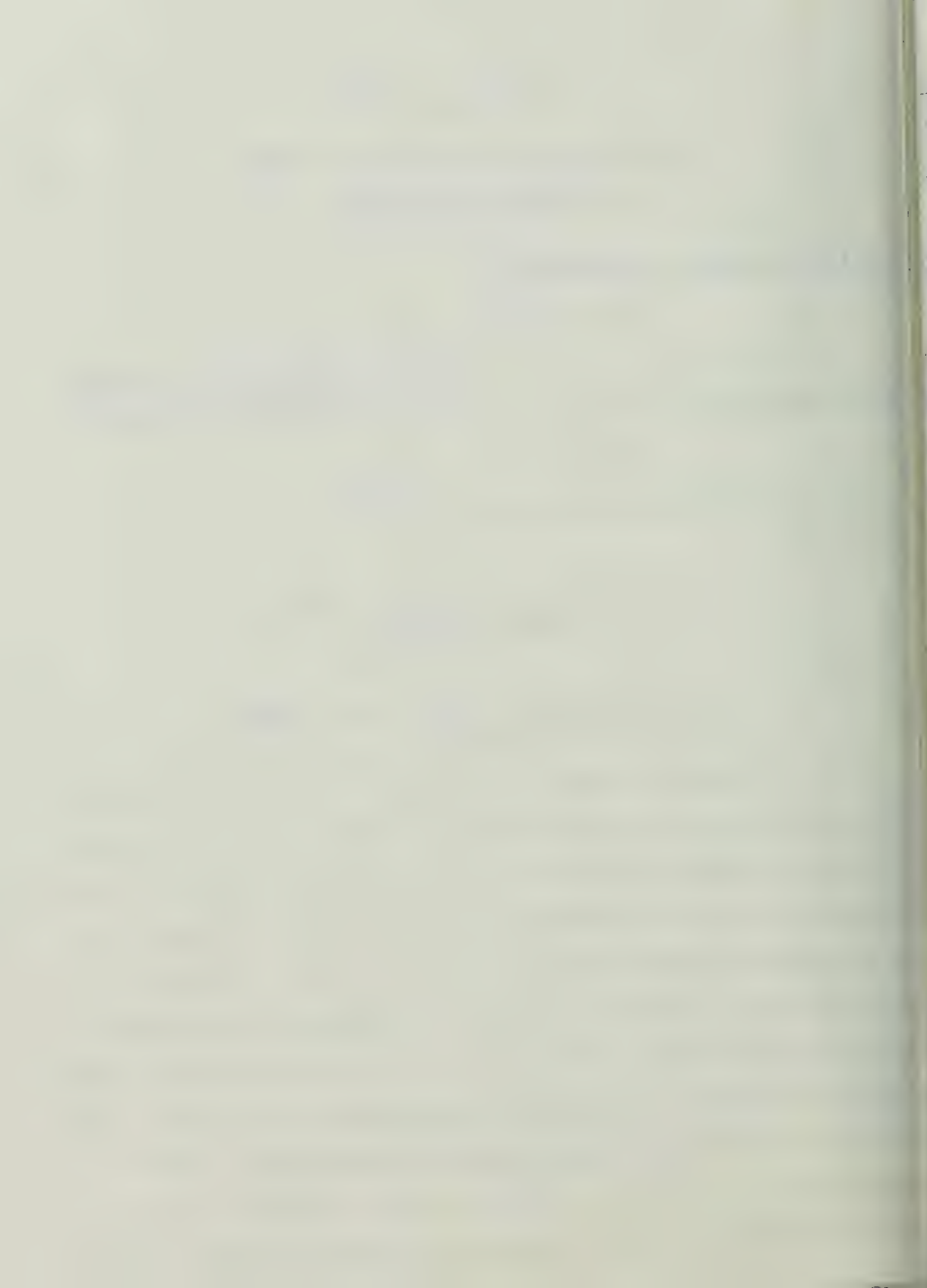
IN THE UNITED STATES COURT OF APPEALS
FOR THE NINTH CIRCUIT

ISLAND AIRLINES, INCORPORATED,)	
)	
Petitioner,)	
)	
vs.)	PETITION TO REVIEW
)	ORDER OF THE CIVIL
CIVIL AERONAUTICS BOARD,)	AERONAUTICS BOARD
)	
Respondent.)	
)	

BRIEF FOR ALOHA AIRLINES, INC.,
AMICUS CURIAE

INTEREST OF AMICUS CURIAE AND SUMMARY
OF ARGUMENT

Aloha Airlines, Inc. (herein "ALOHA") is a Hawaii corporation holding a Certificate of Public Convenience and Necessity (issued to it after proof of public convenience and necessity in 1948) by Respondent (herein "CAB") under § 401 of the Federal Aviation Act of 1958 (72 Stat. 731, 49 U.S.C. 1301 et seq.). Aloha intervened in the applications before the Public Utilities Commission of the State of Hawaii (herein "PUC"), reviewed in In re Island Airlines, Inc., 44 Haw. 634, 361 P.2d 390 (1961); In re Island Airlines, Inc., 47 Haw. 1 and 47 Haw. 87, 384 P.2d 536 (1963); it intervened, filed a brief and presented oral argument in Island Airlines, Inc. v.



Cas., 352 F.Sd 121 (1964), which affirmed the injunction issued at the suit of CAB by the United States District Court for Hawaii (235 F.Supp. 990 (D.Haw. 1964)).

This brief as amicus is filed pursuant to Order of the Court granting leave on February 9, 1966.

Aloha views the application for blanket exemption as an attempt in effect by Petitioner to require CAB to decertify Aloha on an unsupported showing that this is required by "deference" toward state sovereignty where Federal jurisdiction rests on a "purely technical" basis (R. 20-24) and on a claim that there can be no Federal interest "in protecting the two existing air carriers from competition." The analytical brief filed for CAB (in which brief Aloha joins) answers the substantive contentions made in the petition and demonstrated fully that there was no irregularity in the CAB's procedures.

Aloha will limit itself herein to a showing that:
(1) within the existing Hawaiian regulatory framework covering public utilities, to surrender (by exemption) the jurisdiction to license and regulate inter-island air transportation to the State of Hawaii, would on the record before this Court be, in effect, a revocation of Aloha's certificate and such revocation is permitted by Federal law only for intentional violations of the Act (Section 401(g), 49 U.S.C. 1371(g)), and (2) the exemption, if granted, would in effect be placing Aloha's business in a regulatory void and would cripple the existing certificated carriers and destroy for the interstate passengers as well as

intrastate passengers the existing air service all without a record showing of "any facts which would indicate that existing services are inadequate to meet the air service needs of Hawaiian residents" (R. 168).

STATUTES INVOLVED

Relative provisions of the Federal Aviation Act of 1958 (72 Stat. 731, as amended, 49 U.S.C. 1301, et seq.,) are reproduced in the brief for CAB. In addition, reference is made herein to Section 401(g) which reads as follows:

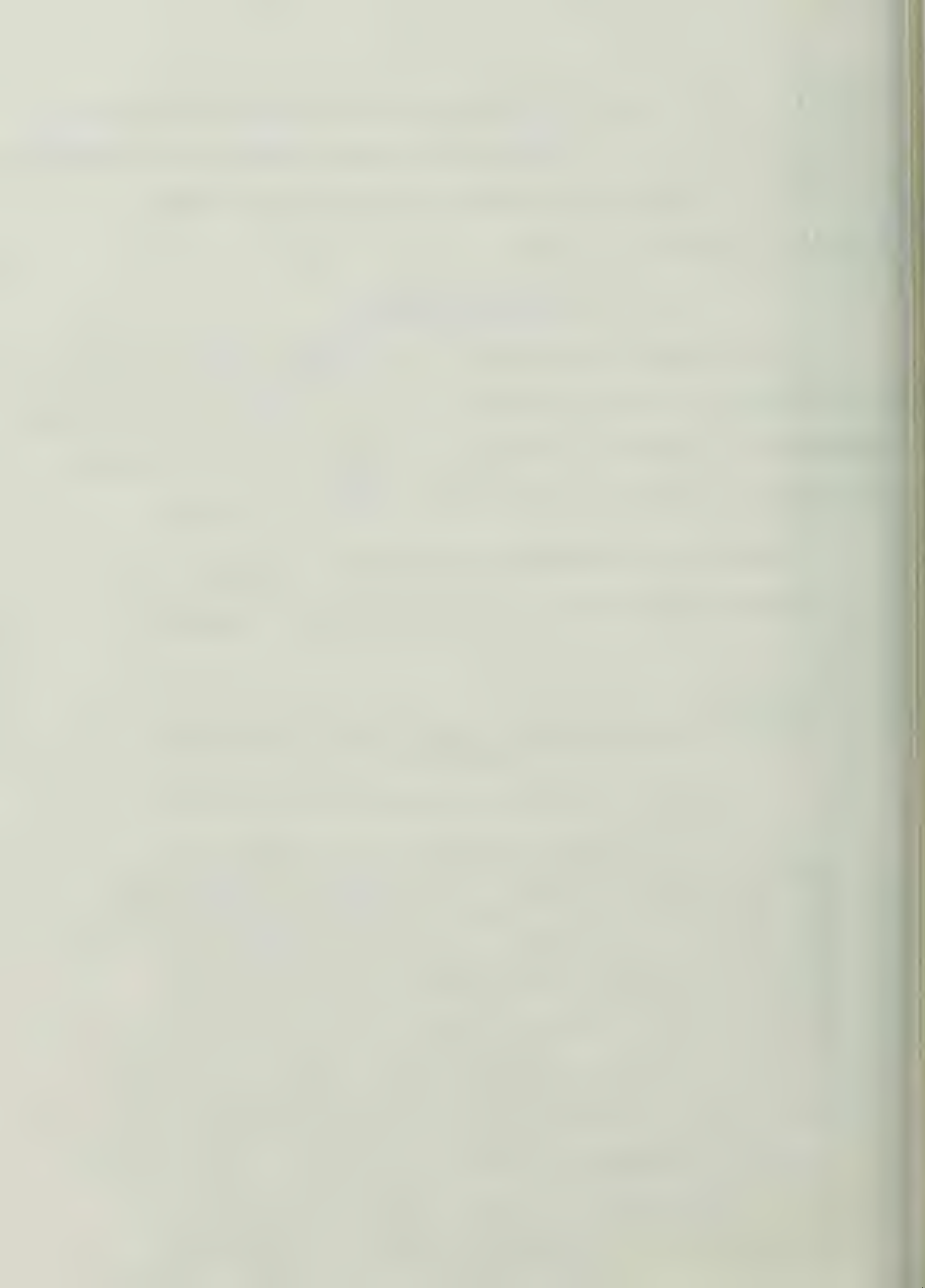
TITLE IV - AIR CARRIER ECONOMIC REGULATION CERTIFICATE OF PUBLIC CONVENIENCE AND NECESSITY

* * * *

Alteration, amendment, modification, suspension,
or revocation

Sec. 401. [72 Stat. 754, 49 U.S.C. 1371]

"(g) The Board upon petition or complaint or upon its own initiative, after notice and hearings, may alter, amend, modify, or suspend any such certificate, in whole or in part, if the public convenience and necessity so require, or may revoke any such certificate, in whole or in part, for intentional failure to comply with any provision of this subchapter or any order, rule, or regulation issued hereunder or any term, condition, or limitation of such certificate: Provided, That no such certificate shall be revoked unless the holder thereof fails to comply, within a reasonable time to be fixed by the Board, with an order of the Board commanding obedience to the provision, or to the order (other than an order issued in accordance with this proviso), rule, regulation, term, condition, or limitation found by the Board to have been violated. Any interested person may file with the Board a protest or memorandum in support of or in opposition to the alteration, amend-



ment, modification, suspension, or revocation of the certificate."

I

THE BLANKET EXEMPTION WOULD AMOUNT TO A
DECERTIFICATION OF ALOHA CONTRARY TO SECTION
401(g) OF THE FEDERAL AVIATION ACT OF 1958
(49 U.S.C. 1371(g)).

The Petitioner has heretofore unsuccessfully urged upon this Court its view that Federal agencies and the Court should refrain from exercising their Congressionally granted powers and duties because of the Hawaiian Supreme Court's decision upholding the PUC's jurisdiction over air transportation between the islands. The present position of the Petitioner can be paraphrased by the conclusion contained in the brief of State of Hawaii, Amicus Curiae:

"However competent and well-meaning a Federal agency such as the Civil Aeronautics Board may be, it cannot be denied that a State agency acutely sensitive, aware and attuned to ever changing local needs and conditions can provide more effective and meaningful controls and regulations for Hawaii's air-transportation problems." (State Br. p. 5)

Assuming, arguenda, there could be a factual basis for the political argument contained in the State's conclusion, we submit to this Court that Aloha with its huge investment in providing a public service, cannot legally be decertificated upon the basis of the political considerations contained in the State's brief. The State, through its elected representatives and through its governmental machinery, has a continuing opportunity to address the Congress of the United States. Before the law making body, Aloha believes it could be abundantly

demonstrated that the State's position is not supportable and a statutory change of responsibility would ultimately militate against the economic well-being of these islands. In this Court proceeding, however, we feel it our duty merely to call attention to the legal requirements that might impel a court to overturn the administrative determination made by CAB.

In determining whether this court should overturn the CAB's determination that Petitioner has "not shown that the enforcement of the provisions of Title IV of the Act is an undue burden upon Island by reason of the limited extent of or unusual circumstances affecting its operations, and would not be in the public interest" (R. 168 (finding of CAB)), the nature of Petitioner's operations in Hawaii as disclosed by the record are considered:

A. Island has not only denied consistently CAB jurisdiction and flown in violation of Federal law (which flaunting of the law resulted in the injunction affirmed by this Court (352 F.2d 735), but it has operated in violation of State law. [See the background of the operations set forth in Hawaiian's answers R. 40-43.]

B. The PUC in denying to Island an interim Order to permit it "to continue the intrastate transportation of passengers by air between the islands of the State of Hawaii" (R. 140) specifically found that all of Island's operations to this date as a carrier by air have been unauthorized under State law.

"The record is abundantly clear that the Commission, in approving Island Airlines' original application on July 26, 1962, did so on a schedule proposed by the Applicant for a six-island, three-plane operation and a capitalization authorized at \$250,000. Applicant has indicated in this record that in beginning commercial operations about a month and a half ago, it did so on a one-plane, four-island basis, without prior approval of this Commission. While the Commission does understand and is sympathetic with Applicant's difficulties with the Civil Aeronautics Board, the Federal Aviation Agency and the Federal Government, it has never authorized Applicant's one-plane, four-island operation." (PUC: Decision & Order No. 1227, R. 140, 141)

CAB has cogently dealt with (CAB Br. pp. 23-34)

Island's "constitutional policy arguments" and arguments that the public interest calls for preservation of local power over local commerce. CAB points out that the Board specifically dealt with this question [in this exemption proceeding], finding that it had been disposed of by Congress itself. (R. 168-169)

We deal here with the Hawaiian regulatory statutes. The Hawaiian statutory scheme for regulation of public utilities has not been substantially altered since Congress dealt with it at the time of statehood. The Hawaiian Supreme Court has recognized (384 P.2d 536, 545) that under State law the PUC has a duty to compel compliance of locally operating utilities with Federal law.

"As amended Chapter 104, R.L.H. 1955, conferred upon the Commission inter alia the following powers:

'5. To "examine into the condition of each public utility, * * * its compliance with all applicable [State] and federal laws * * * and all matters of every nature affecting the relations and transactions between it

and the public or persons or corporations." Sec. 104-6. To examine into such matters "notwithstanding that the same may be within the jurisdiction of the interstate commerce commission, or within the jurisdiction of any court or other body, and when after such examination the commission is of the opinion that the circumstances warrant, it shall effect the necessary relief or remedy by the institution and prosecution of appropriate proceedings or otherwise before the interstate commerce commission, or such court or other body, in its own name or in the name of the [State], or in the name or names of any complainant or complainants, as it may deem best." Sec. 104-14."

The Supreme Court also points out that State certifying procedure was not in effect,

"But Federal certification procedure was in effect, and the record was such that under RLH §§ 104-6 and 104-14 as set forth in paragraph J, supra, the Commission had the power and the duty to examine into, and of necessary effect, compliance with the Federal law by all available means . . . we cannot agree that under our statute the Public Utilities Commission has no responsibility with respect to Compliance with Federal law. See *Inter-Island Steam Nav. Co. v. Territory*, 305 U.S. 306, 59 S.Ct. 202, 83 L.Ed. 189, aff'g 96 F.(2d) 412 (9th Cir.) which aff'd 33 Haw. 890; *Territory v. Inter-Island Steam Nav. Co.*, 32 Haw. 127." 384 P.2d 536, 541.

It seems abundantly clear that under the existing statute local interests are fully protected by permitting and directing the State agency to be the watchdog over the now admittedly Federally regulated business in which Island seeks to engage. The State agency has full power "to effect compliance with Federal law by all available means." This State machinery (and all other legal machinery available to the State) has been completely ignored and the applicant asks this Court to help it by supplying a

"sledge hammer" exemption. What is needed is an orderly, factually supported application, by Island to CAB for a Federal certificate, something it has had ample time (but no inclination) to apply for.

As pointed out by CAB (Br. p. 20) Hawaiian and Aloha operate as part of the National air transportation system. The National system under Congressional regulation is adapted to the needs of the "'foreign and domestic commerce of the United States, of the Postal Service, and of the National defense.'" The development of such a National system has made it mandatory in most cases that local carriers be supported by subsidies and the Federal government has a substantial interest in the problems of inter-island air transportation because of subsidies paid since 1949. The State has not made, and in all probability could not, provide comparable subsidies to the end that (in the interest of all of the citizens of all of the United States) there be provided a service comparable in standard to that maintained by the inter-island certificated air carriers at the present time. To ignore the diversionary impact of competitive service on the established Federally certificated carriers is not only irresponsible public utility regulation, but flies in the face

of a National policy established by the Congress.^{1/}

II

THERE IS NO STATE CERTIFICATING AUTHORITY UNDER EXISTING STATUTES.

The State of Hawaii, Amicus Curiae, urges that it not only has the jurisdiction but also the necessary laws and machinery to regulate properly the inter-island air transportation service in the State of Hawaii (State Br. Amicus Curiae, p. 2).

In 1962, the State legislature of Hawaii, in mistaken reliance upon the jurisdiction asserted by the State, has given the PUC the authority to control the entry of air carriers in Hawaii by the issuance of certificates of public convenience and necessity (Sec. 3, Act 25, Session Laws of Hawaii, Regular Session 1962) subject only to the proviso that the exercise of this certificating authority shall be ineffective until such time as there has been a final determination by the courts that the PUC does as a matter of law have jurisdiction over air

1 The United States District Court ruled in favor of the CAB and issued a permanent injunction against Island on August 8, 1963. The supplemental opinion of the Hawaii Supreme Court had remanded Island's application to the PUC for further hearings and for findings on the effect of the operation upon the Federally certificated carriers. The months of hearings that are referred to in the State brief occurred in a period after a Federal court had determined that the PUC had no jurisdiction, the State taking the position that the supremacy clause of the Constitution was in no way applicable to an administrative proceeding.

transportation service.^{1/}

It is clear within the existing statutory framework of Act 25, supra, as expressly determined by the PUC^{2/} that it does not presently have certificate issuing authority. Consequently, statutes of Hawaii do not presently afford or even permit the proper regulation of the air transportation service within the State of Hawaii and the obvious outcome of the relinquishment in toto of regulation by the CAB would be a chaotic air transportation service unlimited in new entries.

The factual material contained in the State's brief (pages 4 and 5) demonstrates that the State presently does not have the necessary machinery to regulate inter-island air transportation if such air transportation is to conform to the standards which have been maintained under Federal regulation.

The PUC, as appointed by the State, is made up of commissioners who serve "efficiently on a part-time, staggered-term basis for nominal compensation." Their only experience with the economic regulation of air carriers is that reflected in the present record, and this indicates the regulatory void that would exist were the blanket exemption granted. Aloha has,

1 This proviso provides in part as follows: "Section 3 of this Act shall take effect immediately upon the final determination by the courts that the Public Utilities Commission of the State of Hawaii has jurisdiction to regulate air carriers operating between the eight major islands of the State."

2 See PUC Decision and Order No. 1502, Docket No. 1463, filed April 13, 1965 (In the Matter of the Application of Island Airline Inc. for Approval of Rates) (Referred to R:39).

over objections made to the jurisdiction of the PUC, been subjected to the months of prolonged PUC hearings referred to in the State Brief (State Br. p. 4). In these hearings, in great detail, statistical data with respect to inter-island traffic, operating costs, fares, service and estimates of the effect of third carrier competition were presented to the PUC pursuant to the 1963 remand order of the Hawaii Supreme Court in In re Island Airlines, Inc., supra. Even after the injunction had been granted by the United States District Court,^{1/} the State insisted that PUC hearings nevertheless continue and these ultimately resulted in the determination by the PUC, embodied in Decision and Order No. 1502, February 1, 1965 (R. 39). This Order is paraphrased by the State in its brief as follows:

"Decision and Order 1502 filed February 1, 1965, by the Hawaii Public Utilities Commission came after months of prolonged hearings, testimony and other evidence submitted by Island Airlines and the C.A.B. certified carriers--Hawaiian and Aloha Airlines. This authorization issued by the Commission on February 1, 1965, approving Island Airlines' proposed rates and charges authorized Island Airlines to operate on the proposed schedules and rates for a test period of one year beginning six months after the effective date of the order, or such extensions as the Commission might grant. . . ."

An appeal was taken by Aloha to the Supreme Court

¹ The catastrophic impact on the inter-island carriers is summarized in the answer filed before the CAB by Aloha (R. 148-158). The Deputy Attorney General for the State who signed the brief amicus acted in the same capacity as attorney for the PUC.

of Hawaii from this Order, and the State on October 29, 1965, filed its motion for an order dismissing the appeal on the ground that the order of the PUC was an "interim" not a "final" order and therefore could not be appealed from. After this Court filed its decision on October 29, 1965 affirming the injunction of the United States District Court, a motion was filed by Aloha on January 25, 1966 in the Supreme Court for an order to remand the PUC proceeding back to the Public Utilities Commission. This motion for remand was resisted by the State (who insisted that the appeal should be dismissed) and is still pending before the Supreme Court.

Section 401(g) of the Federal Aviation Act specifically provides in substance that the Board shall not revoke a certificate in whole or in part except for an intentional failure to comply with the laws or regulations thereunder or with an order specifically commanding obedience to a provision, order, rule, regulation, term, condition or limitation found by the Board to have been violated. In effect, this means that a revocation of the certificate cannot be effected without proof of a wilful violation, and in Pan Am. World Airways, Inc. v. Boyd, 207 F.Supp. 152 (D.C.D.C. 1962), it was held that the Board may not achieve by indirection that which it is powerless to accomplish directly, it may not avoid statutory restriction on its authority to revoke a certificate. Not only is there no basis for the granting of a statutory exemption, but for the CAB to abdicate its jurisdiction on the basis of the record before this Court in favor

of the State would be the equivalent of an indirect revocation of the certificate heretofore given to Aloha.


It is abundantly clear that there is at the present time no State certifying authority for air carriers engaged in inter-island air transportation and that the blanket exemption would therefore in effect amount to a decertification of Aloha in violation of the Federal statute.

CONCLUSION

Neither the Petitioner nor the State has presented to this Court a basis upon which the CAB could be asked to relinquish to the State its jurisdiction to regulate inter-island air transportation in Hawaii. A fortiori no record has been made out upon which this Court could make its determination that the CAB order is wrongful. The entry of a blanket exemption as prayed for by the petition would result in an indirect decertification of Aloha in violation of Federal law.

WHEREFORE, it is respectfully submitted that the Board's order should be affirmed.

Dated: Honolulu, Hawaii, April 12, 1966.


J. Russell Cades

Attorney for Aloha Airlines, Inc.,
Amicus Curiae

Of Counsel:

SMITH, WILD, BEEBE & CADES

FEB 14 1967

NO. 20552

IN THE UNITED STATES COURT OF APPEALS

FOR THE NINTH CIRCUIT

ISLAND AIRLINES, INCORPORATED,)

Petitioner,)

vs.)

CIVIL AERONAUTICS BOARD,)

Respondent.)

PETITION TO REVIEW
ORDER OF THE CIVIL
AERONAUTICS BOARD

BRIEF OF AMICUS CURIAE
HAWAIIAN AIRLINES, INC.

FILED

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U.S. COURT OF APPEALS

ALLEN M. STACK
1100 First National Bank Bldg.
Honolulu, Hawaii

Attorney for HAWAIIAN AIR-
LINES, INC., Amicus Curiae

PRATT, MOORE, BORTZ & VITOUSEK
Of Counsel

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BRIEF OF AMICUS CURIAE
HAWAIIAN AIRLINES, INC.

SUMMARY OF ARGUMENT

A. The decision of this Court in the injunction proceeding, which is related to this proceeding, Island Airlines v. C.A.B., 352 F.2d 735 (9th Cir. 1965), has already rejected Island Airlines' contention in its second specification of error that -

Denial of exemption was unlawful because it extinguished Hawaii's power over its intra-state commerce in derogation of Hawaii's "equal

footing" with other states under the U.S. Constitution and the Hawaii Statehood Act. (p. 4, Petitioner's Brief)

B. The continued policing by the Civil Aeronautics Board which is required in California to prevent an intrastate airline from carrying interstate passengers (persons whose journeys commenced or terminated at points outside of California) is adequate reason for the Board's denial of exemption of a proposed operation which could create the same problems.

ARGUMENT

I. DENIAL OF EXEMPTION DOES NOT DEPRIVE THE STATE OF HAWAII OF "EQUAL FOOTING" IN THE FEDERAL UNION.

The decision of this Court in the injunction proceeding, which is related to this proceeding, Island Airlines v. C.A.B., 352 F.2d 735 (9th Cir. 1965), has already rejected Island Airlines' contention in its second specification of error that -

Denial of exemption was unlawful because it extinguished Hawaii's power over its intrastate commerce in derogation of Hawaii's "equal

footing" with other states under the U.S. Constitution and the Hawaii Statehood Act. (p. 4 Petitioner's Brief)

In that decision (352 F.2d 735 at p. 744), this Court stated:

We find no "invidious discrimination" against the State of Hawaii in the court's decision below. "Equal boundaries to each state are not necessary." United States v. Louisiana, 363 U.S. 1, 77 (1960).

This Court's decision in the injunction proceeding used the phrase "invidious discrimination" rather than "equal footing," but they were undoubtedly synonymous in the Court's mind. The case cited by the Court, United States v. Louisiana, supra, does not use the phrase "invidious discrimination," but does use the phrase "equal footing" at the cited page. However, the phrase "invidious discrimination" was used by Island Airlines in its brief in the injunction proceeding dated December 24, 1964, on page 3 in the statement of points to be relied upon on appeal, which states as follows:

The Court below erred in not holding that appellee's construction and application of the Federal Aviation Act resulted in unconstitutional and invidious discrimination against Hawaii, her people and appellant.

In the same brief (pp. 92-95), Island specifies as error -

The invidious discrimination against Hawaii and its people by appellee makes its application and construction thereof unconstitutional.

In this specification of error, Island cites one case in support of the invidious discrimination argument, Coyle v. Oklahoma, 221 U.S. 559 (1911). Coyle, however, nowhere mentions "invidious discrimination," but does discuss "equal footing."

From an examination of the briefs on both sides and the Court's opinion in the injunction proceeding, it is clear that the Court did, as the Civil Aeronautics Board contends, reject the equal-footing argument as it applies to this case:

1. Island's brief talks in terms of "invidious discrimination," but in support thereof cites the case Coyle v. Oklahoma, supra, which discusses equal footing.

2. The Civil Aeronautics Board brief talks in terms of "equal footing" and cites, among other cases,

United States v. Louisiana, supra, which also talks in terms of "equal footing."

3. The Court in the injunction proceeding ruled that there was no "invidious discrimination" against the State of Hawaii, but the case it cited in support thereof, United States v. Louisiana, supra, talks only in terms of "equal footing."

In view of the foregoing, it is obvious that although the Court in the injunction proceeding decision spoke of invidious discrimination, it was in fact disposing of the equal footing argument advanced by Island Airlines in that proceeding.

The United States Court of Appeals for the Ninth Circuit was correct in rejecting Island's equal-footing argument because that doctrine has never required that the various states be treated equally in every respect. For example, United States v. Louisiana, supra, cited by both the Civil Aeronautics Board and the Court, provides as follows:

. . . Nor does the concept of equal footing require such a construction. While the ownership

of certain lands within state boundaries has been held to be an inseparable attribute of the political sovereignty guaranteed equally to all States, see United States v Texas, supra (339 US at 716), the geographic extent of those boundaries, and thus of the lands owned, clearly has nothing to do with political equality. (p. 77)

Another Supreme Court case discussing equal footing is Alabama v. Texas, 347 U.S. 272 (1954). That case provides as follows:

The fact that Alabama and the defendant states were admitted into the Union "upon the same footing with the original states, in all respects whatever," 2 Stat 701, 3 Stat 489, 5 Stat 742, 797, 9 Stat 452, does not affect Congress' power to dispose of federal property. The requirement of equal footing does not demand that courts wipe out diversities "in the economic aspects of the several States," but calls for "parity as respects political standing and sovereignty." United States v. Texas, supra (339 US at 716). The power of Congress to cede property to one state without corresponding cession to all states has been consistently recognized. See, e.g., United States v. Wyoming, 335 US 895, 93 L ed 431, 69 S Ct 297, and cases cited by the Court. (p. 275)

Another case discussing equal footing is United States v. Texas, 339 U.S. 707 (1950). A portion of the Court's opinion follows:

. . . We are of the view that the "equal footing" clause of the Joint Resolution admitting Texas to the Union disposes of the present phase of the controversy.

The "equal footing" clause has long been held to refer to political rights and to sovereignty. See *Stearns v. Minnesota*, 179 US 223, 245, 45 L ed 162, 174, 21 S Ct 73. It does not, of course, include economic stature or standing. There has never been equality among the States in that sense. Some States when they entered the Union had within their boundaries tracts of land belonging to the Federal Government; others were sovereigns of their soil. Some had special agreements with the Federal Government governing property within their borders. See *Stearns v. Minnesota*, supra (179 US pp 243-245, 45 L ed 173-175, 21 S Ct 73). Area, location, geology, and latitude have created great diversity in the economic aspects of the several States. The requirement of equal footing was designed not to wipe out those diversities but to create parity as respects political standing and sovereignty.

Yet the "equal footing" clause has long been held to have a direct effect on certain property rights. Thus the question early arose in controversies between the Federal Government and the States as to the ownership of the shores of navigable waters and the soils under them. It was consistently held that to deny to the States, admitted subsequent to the formation of the Union, ownership of this property would deny them admission on an equal footing with the original States, since the original States did not grant these properties to the United States, but reserved them to themselves. . . . (pp. 715-716)

Federal regulation that is otherwise valid is not

a violation of the "equal-footing" doctrine merely because its impact may differ between various states because of geographic or economic reasons. United States v. 43 Gallons of Whiskey, 93 U.S. 188, 197 (1876).

II. THE CONTINUED POLICING WHICH EXEMPTION WOULD REQUIRE IS ADEQUATE REASON FOR DENIAL OF EXEMPTION.

The continued policing by the Civil Aeronautics Board which is required in California to prevent an intra-state airline from carrying interstate passengers (persons whose journeys commenced or terminated at points outside of California) is adequate reason for the Board's denial of exemption of a proposed operation which could create the same problems.

In California there are airlines which operate without a Civil Aeronautics Board certificate of public convenience and necessity because they fly only within the boundaries of the state, and they have represented that they do not carry substantial numbers of interstate passengers. C.A.B. v. Friedkin Aeronautics, 246 F.2d 173 (9th Cir. 1957). On this basis, they are beyond the reach of the Board's

economic regulation. Where the geographic factor is lacking, similar carriage in California has been subjected to the Board's economic regulation. United Airlines, Inc. v. P.U.C., 109 F.Supp. 13 (N.D.Cal. 1952), rev'd on other grounds, 346 U.S. 402 (1953).

Respondent's brief in this proceeding, in footnote 23 on page 22, points out that a cease and desist order has been issued against the carrier involved in the Friedkin case, supra.

The situation in Hawaii is similar in that substantial numbers of tourists and other interstate passengers fly between the Hawaiian Islands and a similar policing problem would be bound to develop if the exemption requested by petitioner were to be granted.

CONCLUSION

The declared policy underlying the Federal Aviation Act of 1958, which is set forth in Section 102, 49 U.S.C. 1302, contemplates a national air transportation system regulated by the Civil Aeronautics Board. The juris-

dictional sections of the Act are designed to extend the jurisdiction of the Board to the utmost within the limits of the Commerce Clause of the United States Constitution. In California the Board has been thwarted by the geographical factor in extending its economic regulation to certain airlines and has been forced into the role of a policeman attempting to prevent the "intrastate" airlines from carrying interstate passengers. The State of Hawaii has a geographical situation which precludes such a limitation on the Board's jurisdiction and thereby furthers the policy of the Federal Aviation Act.

DATED: Honolulu, Hawaii, April 11, 1966.

Respectfully submitted,

ALLEN M. STACK

ALLEN M. STACK
1100 First National Bank Bldg.
Honolulu, Hawaii

PRATT, MOORE, BORTZ & VITOUSEK
Of Counsel

Attorney for HAWAIIAN AIR-
LINES, INC., Amicus Curiae

